BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI

In the Matter of Laclede Gas Company's Request to Increase Its Revenues for Gas Service	))	**File No. GR-2017-0215** Tariff No. YG-2017-0195
In the Matter of Laclede Gas Company d/b/a Missouri Gas Energy's Request to Increase Its Revenues for Gas Service	)))	**File No. GR-2017-0216** Tariff No. YG-2017-0196

REPLY BRIEF OF

SPIRE MISSOURI INC.

JANUARY 17, 2018

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REPLY BRIEF OF SPIRE MISSOURI INC

Spire Missouri Inc. (f/k/a Laclede Gas Company and referred to herein as "Spire Missouri" or "Company") respectfully submits its Reply Brief on behalf of its operating units Spire Missouri East (f/k/a Laclede Gas Company and referred to herein as "LAC") and Spire Missouri West (f/k/a Missouri Gas Energy and referred to herein as "MGE") in accordance with the Commission's *Order Adopting Procedural Schedule and Delegating Authority* issued in this matter on May 24, 2017. The Company will reply to the briefs of the other parties on the remaining contested issues in this case using the same numerical sequence appearing in the *Amended List of Issues, Order of Witnesses, Order of Cross-Examination, and Order of Opening Statements* filed by Staff on December 1, 2017.

INTRODUCTION

The most notable aspect of the briefs filed by the other parties in this proceeding is the complete absence of any argument contesting the extraordinary record Spire Missouri has compiled on behalf of its customers over the past several years. JW Marriott once said "if you take care of your people, your people will take care of your customers and your business will take care of itself." Consistent with that maxim, Spire agrees that aligning the interests of employees, customers and business is a good thing, and that creates opportunities for mutually beneficial outcomes and more sustainable success for all stakeholders. Along those lines, we believe that good policy by the Commission would seek the same, align the interests of the

stakeholders and create benefits for all, rather than assuming that it is a "zero sum game" where benefits can only be created through detrimental positions on the other participants.

With faith in the basic fairness of Missouri regulators, debt and equity investors committed hundreds of millions of dollars to purchase MGE, $210 million of which is excluded from rate base and will never earn a regulated return. Similarly, Spire employees also invested considerable thought. hard work and long hours focusing on improving the outcome for both the Company and its customers. Through the integration work of numerous employees, that investment has now been transformed into $50 million in ongoing savings, all of which have been reflected in the cost of service for MGE or LAC in these cases. Over and above that, they have created another $19 million in savings related to Alagasco and EnergySouth. IT systems were built to provide MGE with a badly-needed, state-of-the-art information management system at a mere fraction of the $80 million cost LAC incurred just two years before to build and install the same system for itself. Work on the St. Peters lateral project positioned the LAC to obtain discounts from its pipeline supplier that will be worth $54 million in savings to customers over the next 12 years. Investors also provided $16.6 million for employees to purchase the AMR devices serving LAC, so that customers could begin receiving nets savings of $1 million or more a year as a result of lower-meter reading expenses. The Company's finance employees also played a critical role by assertively pursuing tax deductions which have generated $100 million alone in rate base reductions in these cases. No party disputes in their initial briefs that these savings and efficiencies have been achieved, because the evidence won't let them.

Nor have they disputed in their briefs the significant service enhancements the Company and its employees have achieved at the same time these financial benefits have been created. These achievements span the entire spectrum of the Company's employee base, from

union witness Mark Boyle, who testified that field personnel have improved the way they approach engagements with customers, to Spire Missouri's President, Steven Lindsey, who testified that performance has improved in virtually all areas of operations and customer service. The Company knows this because it measures them, and what gets measured, gets done. (Tr. 495). The Company and its employees respond to leaks faster; remove cast iron faster; address stopped meters faster; answer the phone faster; and communicate with customers better.

Instead, the positions expressed in the briefs submitted by Staff, OPC, MIEC, MEIG and certain other parties in response to this record of achievement on behalf of customers read like an indictment – a case study in how truly dysfunctional regulatory advocacy can be, and how ardently they cling to the belief that one stakeholder must suffer so that other may benefit, or in this case, further benefit. One will search these briefs in vain for any acknowledgement of, let alone appreciation for, the enhancements to the business, improvements to customer service and tens of millions of dollars in cost reductions the Company has brought to its customers. Rather, in return for these benefits, they heap one opportunistic and punitive adjustment on top of another, as if to impress upon the Company the negative consequences of such activities.[1]

They begin with an attempt to effectively fine the Company more than $20 million through capital structure adjustments that would reduce its equity component far below the level that has been historically used to set the Company's rates and that is embedded in the capital

[1]It is particularly disappointing to see the Staff join in this unwarranted and excessive series of adjustments, especially in view of its asserted role as an independent party "that is above any specific interest" and that is supposed to provide the Commission with "neutral, yet expert" advice rather than be a consumer advocate. (***In the Matter of the Joint Application of Hickory Hills Water & Sewer Co., Inc. and Missouri-American Water Company***; Order Denying Request for Local Public Hearings and Granting Applications with Conditions, WA-2016-0019, dated November 4, 2015; *See also* Commission website).

structures of the Company's peer utilities. They continue their punitive exercise with proposed adjustments like the attempt to confiscate a significant share of the proceeds realized by the Company from the sale of its Forest Park facilities. Staff affirmatively concludes that the Company acted prudently in selling Forest Park, but then relies on irrelevant and incorrect factual assertions in recommending significant adjustments, including that the sale was not a land-only transaction (it was), that the cost to construct the Manchester facility was higher than the cost to stay at Forest Park (it wasn't), and that the relocation proceeds hadn't been spent (they had). (Staff Brief, pp. 12, 13, 15).

Staff and OPC have also proposed that the Company, in contrast to every other gas utility in Missouri, receive a return of approximately 1.5% on its gas storage inventories as the price for moving them into base rates and taking on all the carrying cost risk of rising interest rates and gas prices. In incentive compensation, Staff disallows all management AIP incentives, even though earnings based and performance metrics were part of an overall incentive program that was the driving force behind the significant cost reductions and service enhancements that benefit customers. In doing so, Staff failed to mention, the Commission's most recent 2009 Ameren decision on this issue that allowed earning based metrics as part of a balanced scorecard, boasting instead about how it reversed that policy decision through a subsequent settlement. Likewise, with pensions, Staff seeks to eliminate nearly $30 million in pre-paid pension asserts from rates incurred for the benefit of Company's employees based on partial and contradictory information.

Unfortunately, the counterproductive positions taken by the Staff and other parties do not end with revenue requirement issues. Staff and OPC oppose the statutorily authorized Revenue Stabilization Mechanism and tracker for environmental remediation costs. In its alternative proposal, Staff suggest that the Commission adopt an approach to weatherization

normalization that would actually make the Company and its customers significantly *more* exposed to the effects of weather than they are today – while then arguing for no transition rates and a reduction in ROE.

It is not clear why the Staff, OPC and certain other parties have taken such extreme positions, but what is clear is that the sum and substance of their adjustments results in the Company not being able to recover its prudently incurred costs – costs which were integral to the benefits customers enjoyed with enhanced service level, a rate case that was deferred and rates that are lower than they were ten years ago. It is telling that parties now assume the Company will be on a four-year rate cycle, when the history prior to this period of achievement on behalf of customers was every two or three years. Nevertheless, they now try grab further rate reductions in an unprecedented manner while simultaneously diminishing or ignoring the costs that were incurred to achieve that benefit.

In the end, when evaluating the legitimacy of these arguments and adjustments, the Commission should bear in mind how the Company has managed for nearly eight hears to avoid any increase other for safety and public improvement investments made under ISRS. The increase has been zero for inflation, including our employees' wages, salaries, incentives, pension expenses, along with other operations and maintenance costs. The increase has also been zero for non-ISRS capital, all of which began to depreciate as soon as they went into service, including two enterprise-wide information systems brought online in 2013 and 2015 for LAC and MGE, respectively. In other words, over the past eight years, our people have delivered to our customers better service and increased safety, all for no increase in rates other than for our ISRS safety and relocation costs.

All the Company asks for in return is for fair treatment on the remaining issues, the benefit of the doubt on a few close questions, and maybe a thumbs-up for eight years of work well done.

The Company sincerely believes its performance on behalf of customers over the past several years has earned this kind of response. If the Commission wishes to see more mutually beneficial outcomes, it should consider approving positions and adopting policies in these cases that help further align the business, employees and customers. After all, balancing the interests of the stakeholders is aligned with the purpose of the Commission.

ARGUMENT ON SPECIFIC ISSUES

I. LAC Only Issues

a. Forest Park Property

i. How should any gain resulting from the sale of the Forest Park property be treated for ratemaking purposes?

In their respective briefs, neither Staff nor OPC addressed in any substantive way the legal and factual considerations that require rejection of their proposal to take a portion of the gains from the sale of the Forest Park property in 2014. As discussed in the Company's initial brief, the Commission has traditionally treated gains on the sale of utility assets *below* the line. *See* ***Re Kansas City Power and Light Company,*** Case Nos. EO–85–185 and EO–85–224; 75 P.U.R.4th 1 (1986), ***Re Missouri Cites Water Co***., 26 Mo PSC NS 1 (1983) and ***Re Associated Nat. Gas Co.****,* 26 Mo PSC NS 237, 55 PUR4th 702 (1983), especially where, as here, the transaction involves the sale of non-depreciable property such as land. ***Kansas City Power and Light, supra***, at 29.

While, as Staff notes, circumstances may occasionally arise where it is appropriate for a utility to share a gain on the sale of assets with its customers, neither Staff nor OPC have provided anything in their initial briefs to support that such circumstances exist in this case. In fact, the Staff goes out of its way to point out in its brief that it is not claiming that the Company was "in any way imprudent" in how it handled the Forest Park sale. (Staff Initial Brief, p. 14).

Inexplicably, the Staff goes on to state that this key element in assessing the reasonableness of virtually any utility action, is a mere "distraction" in this instance. (*Id*.).

Instead, the Staff seeks to justify its adjustment by suggesting that customers have nevertheless been harmed by the sale – an assertion that is premised on a series of plainly incorrect factual assertions. First, Staff suggests that such harm arises from the fact that the sale of Forest Park "necessitated the construction of a facility [Manchester] at a higher cost to ratepayers." (Staff Initial Brief, p. 15). As Company witness Kopp testified, however, the Manchester satellite facility was never intended to be, and in fact was not, a replacement for the Forest Park facility. (Ex. No. 43, p. 2, lines 10-12). Moreover, as discussed at length in the Company's Initial Brief, a comprehensive analysis conducted by Ms. Kopp (as compared to Staff's limited analysis) shows that the Manchester satellite facilities would have been some $900,000 *less* expensive to own and operate than the Forest Park facility from 2017 to 2020, assuming the costs required to rehabilitate and make the Forest Park facility suitable for future use had been incurred. (Ex. 43, Schedule SMK-S1).

Second, the Staff suggests that its treatment is appropriate because it is similar to the one used when utility vehicles are sold. (Staff Initial Brief, p. 15). Staff's analogy does not hold, however, because unlike utility vehicles, where the utility receives a return on and a return of the value of the asset (through depreciation), the value of the Forest Park sale, and any associated gain, related entirely to the value of the land, as the property was actually worth *less* with the buildings on them. (Ex. 43, p. 3). The Company has never received a return *of* the value of this non-depreciable land from ratepayers and, as the Commission has previously recognized, this factor makes the gain realized on the transaction particularly fitting for below-the-line treatment.

Finally, the Staff makes much of the fact in its brief that the Company did not seek

Commission approval to sell the Forest Park property, even though it continued to use the facilities for a brief period after the sale was consummated. (Staff Initial Brief, p. 13). In making this argument, the Staff seems to be complaining that the Company broke the law and that the Commission should levy a penalty on the Company for having done so by ordering Staff's recommended treatment of the gain. There is a distinct mechanism under Missouri law for handling such matters, however, and it is not a rate case. It is instead the Complaint process set forth in Section 386.390 RSMo. As the Staff well knows, the complaint process has a number of formalities that must be followed to prove a violation of law. In addition, if a violation of law is found, the Commission must authorize its General Counsel to seek any penalties in Circuit Court, penalties that can only be imposed by the Court after the opportunity for another hearing. (Section 386.600, RSMo.) It is wholly impermissible for the Staff to attempt to short-circuit this process by effectively seeking to impose a penalty in this case for what it views as an alleged violation of the statute.

Nor would there be any basis for such a complaint in any event. Staff's reference to utility vehicles in its Initial Brief is helpful in at least one respect. When utilities do purchase, sell or lease such vehicles they do not come to the Commission for approval, even though the vehicles may be in use at the time or even subject to being used in the future (say under a sale, leaseback arrangement). The reason such approval is not sought is because such vehicles are the kind of assets that can be easily replaced with other goods, equipment or facilities widely available in the marketplace. Accordingly, there is no rationale to seek approval from the Commission whenever a vehicle is sold. Indeed, it would be a huge waste of the Commission's resources and time to involve it in the kind of routine management decisions that go into deciding what make, model, color, size and character of vehicle a utility should buy, sell or lease in providing utility service. The same is true of office and service center facilities. Again,

there are clear and abundant substitutes for such facilities in the marketplace, whether they be located in St. Louis, Kansas City, or Joplin. As long as such alternatives are widely available, any particular office or service center facility is not the kind of critical element of a utility's works or system that requires a Commission approval when one facility is substituted for another.

That is not to say that there are never instances where Commission approval is required. To the contrary, in some cases the facilities proposing to be sold are necessary or useful to providing utility service and sufficiently unique or critical that Commission consent should be obtained. An example of this was the Company's proposed sale or transfer of its 880 pipeline that was still being used to provide service and for which there were no readily available substitutes at the time. *See* ***In the Matter of the Application of Laclede Gas Company to Transfer an Asset to Spire Pipeline, Inc***., Case No GM-2017-0018. The Company recognized that the 880 line was a critical component of its works and system and it accordingly filed an application for Commission approval in 2016. (*Id*.). Although the Company ultimately requested that the Commission stay its consideration of the request pending developments at the Federal Regulatory Commission, the important fact is that the Company appreciates when Commission approval is required for a particular transaction and when it is not required.

Finally, the Company would note that it is not the only party who apparently believed that Commission approval for the Forest Park sale was not required. The Company was very open about its intention to sell the Forest Park property and, as previously noted, discussed it with the Commission, Staff and OPC in a formal presentation in May of 2014. The Company also collaborated closely with the Commission's gas procurement department to ensure that that there was a smooth and seamless move of its gas control operations out of Forest Park and into the new 700 Market Street facility. At no time did the Commission, Commission Staff or OPC

ever suggest that Commission approval of the sale was required. Staff's attempt to do so long after the sale was completed should be rejected as should its proposed treatment of the gain.

For its part, OPC offers nothing substantive to support its position on the gain. Instead, OPC simply asserts, without any supporting citation to the record, that adoption of its proposed treatment is necessary to discourage utilities from "gaming" or "manipulating" the system when assets or sold. (OPC Initial Brief, p. 5). The Company is, by now, thoroughly familiar with OPC's practice of throwing out negative characterizations of utility actions when it has nothing substantive to support its position on an issue. Nevertheless, it is somewhat astonishing to see even OPC make such assertions in connection with the Forest Park sale. As the rebuttal and surrebuttal testimony of Company witness Kopp makes abundantly clear, the disposition of these properties was done in a thoughtful, deliberate and, as both Staff and OPC have acknowledged, prudent way. (*See* Exhibits 42 and 43). The sale also permitted the Company to move its employees out of facilities that were increasingly hazardous and unsafe and into more functional facilities that were more accommodating to the effective implementation of the shared service strategy that has enabled the Company to generate tens of millions of dollars in savings for its customers. At the same time, the sale made it possible for CORTEX to attract an important retail institution to its development district. In addition, Spire Missouri was able to offset some of the costs of refurbishing the iconic office building that the Company was moving into in the heart of downtown St. Louis, and to make a significant financial contribution to the Arch revitalization project, all while still upgrading the facilities used to serve customers at a beneficial cost. If this is what gaming or manipulating the system looks like, the Commission should encourage more of it. In the meantime, it should reject OPC's position on this issue.

ii. How should the relocation proceeds from the sale of the Forest Park property, other than proceeds used for relocation purposes or contributed to capital for

the benefit of customers, be treated for ratemaking purposes?

Neither Staff nor OPC attempt to provide a legal, equitable or policy justification for capturing a portion of the proceeds the Company received and spent to relocate its employees as a result of the Forest Park sale. In support of its position, Staff devotes a total of three conclusory sentences in its Initial Brief. Those sentences merely repeat Staff's proposed accounting treatment, its assertion that such treatment effectuates a proper sharing of the proceeds between ratepayers and shareholders, and its claim that sharing the "windfall" of proceeds in this way will help to mitigate "harm to the ratepayers resulting from the higher cost replacement facility." (Staff Initial Brief, p. 15). OPC is equally cryptic in its brief on this issue, although it uses four conclusory sentences to explain why the Commission should seize a portion of these relocation proceeds (which OPC describes as a "non-recurring gain") and use them to offset the cost of the Manchester facility. (OPC Initial brief, p. 6).

Merely repeating conclusory claims while offering no facts or context to the support them, is not a sufficient basis upon which a party should be allowed to prevail. Perhaps Staff and OPC are only going "through the motions" in this summary way because they understand that the record evidence provides absolutely no factual or policy support for what they are suggesting. Specifically, they know that the record shows that every dime of relocation proceeds were spent on moving, relocation, record duplication and other related costs associated with the Company's facility restructuring, except for the capital contribution made for furniture and fixtures at the new 700 Market Building. (Ex. No. 42, Kopp Rebuttal, pp. 8-9). They also know that many of these costs would have otherwise had to have been paid for by customers had the Company not used the relocation proceeds to pay for them instead. Finally, in addition to these inconvenient facts that demonstrate the basic unfairness of their positions, they also know that they are wildly inconsistent with Commission ratemaking

practices. This includes the practice that generally prohibits parties from reaching back well before the test year in a case to grab a one-time, non-recurring revenue event and, without any kind of deferral order in place, use it to reduce ongoing rates. (***State ex rel. Associated Natural Gas Co. v. PSC***, 954 S.W.2d 520 (Mo. App. W.D. 1997). For all of these reasons the positions of Staff and OPC on the treatment of the Forest Park relocation fees should be rejected by the Commission.

II. MGE Only Issues

a. Kansas Property Tax

As noted by OPC at page 6 of its Brief, Staff, MGE, LAC and OPC have all agreed and recommend that the Commission include an allowance of $1,454,069 in rates for Kansas property taxes, which is the average of those taxes from 2009 to 2016. The parties further recommend the existing tracker for such taxes be continued. Since no other party addressed this issue in their initial briefs, the Company has nothing to add on this issue in its Reply Brief.

III. LAC-MGE Common Issues

a. Cost of Capital

EXECUTIVE SUMMARY:

In their initial briefs, the Staff and OPC, joined by MIEC and MECG, continue to pursue extreme positions on the cost of capital, especially in terms of their recommendations on the capital structure that should be used for setting rates. In its initial brief, the Company demonstrated how adoption of these recommendations would result in an equity component for the Company that is some 700 to 800 basis points below the typical equity level that has historically been used to set the Company's rates and that is being used to set the rates of the Company's peer utilities. Additionally, it should be noted that Staff's actual analysis of ROE supported a range of 6.90-7.70% for LAC and MGE; however, this analysis was so far

out of the mainstream that Staff instead borrowed from past positions of the Commission on electric cases to create a range that would then seem more reasonable to the Commission. This ROE would create a pre-tax cost of capital of 7.170-7.770%, when coupled with Staff's out of the mainstream positions on capital structure. Staff's capital structure position includes significant capital from multiple out of state utilities and non-regulated companies, as well as utilizing an **average** level of short-term debt, which it justifies with an unprecedented position requiring a link of gas inventories in rate base to short-term debt in capitalization. Even using the recommended range of 9.00-9.50%, Staff's pre-tax cost of capital is 8.745-9.119%. Similarly, the position from Mr. Gorman for pre-tax cost of capital would be 9.110-9.499%, using Staff's gross-up factor of 1.646.

Purely as a point of reference and context for these extreme positions, as suggested by Mr. Murray, consider the pre-tax return approved in the M&A stipulation GM-2013-0254 of 10.224% for MGE, though this was only applicable to the next rate case GR-2014-0007 (*Id*. at lines 14-16). In contrast to that 10.224%, Mr. Murray's and Mr. Gorman's cost of capital recommendations of 7.170-7.770% / 8.745-9.119% and 9.110-9.499%%, respectively, are over 72 basis points lower at the highest point of both ranges, and over 300 basis points lower at the lowest point. Notably, Mr. Murray observes in his testimony that if the Commission were to adopt the Company's proposed capital structure, with its 54.2% equity component and the high end of Mr. Murray's recommended ROE range of 9.5%, it would produce an ROR of 10.24%, a figure that is less than *2 basis points* above the MGE Stipulation figure of 10.224% (Ex. 5. p. 6, lines 8-10). Using a range of 10.00-10.35%, which accounts for whether or not a flotation and a small size risk premium should be included, the Company's pre-tax cost of capital position would be 10.685-10.993%, less than 50 basis points above that figure on the low side – closer than the positions of both of the other parties.

The Company believes there are sound reasons for a cost of capital that is higher than MGE's in 2014 and the cost of capital currently in use by LAC of 10.41%. These reasons include the significant customer benefits created by the Company since that time, as well as the recent upward trend in ROE's authorized by other state utility commissions. During the latter half of 2017 these ROE's averaged 9.89% (Tr. 1189) (Ex. 40, p. 40).

The difference in positions can only be explained by the (a) inappropriate effort of Staff to use a parent company capital structure that is increasingly inapposite to the operations of Spire Missouri and, for the first time, incorporate in that capital structure short-term debt; and (b) the equally inappropriate attempt by OPC/MIEC to apply a phantom goodwill adjustment to penalize the Company for non-existent capital structure impacts of the MGE acquisition.

All of which goes to demonstrate in very real and understandable terms the degree to which Staff and OPC/MIEC are using the acquisition not to protect ratepayers from financial harm, but as a pretext for driving down the Company's cost of service and inappropriately not allowing it to recover its cost of capital. In doing so, they are violating the Stipulation and Agreement in the MGE acquisition case, which, under Section 3, contemplated that in future ratemaking proceedings, ratemaking measures and adjustments would be considered by the Commission as "necessary to ensure *no impact* from the acquisition premium on rates."

As the above quoted language makes clear, the requirement barring any financial impact from the acquisition works both ways. It is designed to ensure that neither customers nor the Company are adversely affected by prohibiting any impact on rates, whether that impact be beneficial or detrimental.

The goodwill adjustment proposed by Mr. Gorman on behalf of OPC/MIEC is a particularly direct and obvious violation of this requirement. Mr. Gorman acknowledged on cross examination that the Company has not included any of the goodwill generated as a result

of the MGE acquisition in its rate base so it cannot possibly be earning a return on it. (Tr. 1392, lines 9-16) He also acknowledged that the MGE acquisition was financed with slightly more debt than equity (Tr. 1393, lines 3-9) so it is mathematically impossible that it could have increased the equity component reflected in the Company's capital structure. In fact, it would have slightly decreased equity.

The fact that Mr. Gorman's proposed capital structure nevertheless results in an ROR that is nearly 100 basis points below the one deemed reasonable in the MGE acquisition and rate case proceedings cuts through, as only hard numbers can, all of Mr. Gorman's creative but ultimately baseless theories that such an adjustment is necessary to protect ratepayers. In the process it reveals in stark numerical terms what his goodwill adjustment really is – an opportunistic and unjustified attempt to use the goodwill created in the MGE acquisition to affirmatively reduce rates in a manner proscribed by the Stipulation and Agreement in the MGE acquisition case.

In summary, the Company believes that the Commission should consider the Company's pre-tax cost of capital range of 10.69-10.99% to be reasonable, and closer to the benchmark from the MGE acquisition case than the other parties. This would be based upon long-term capitalization that is not only representative of Spire Missouri's actual capital structure of 54.2% equity and 45.8% debt, but it is in line with previously levels approved for the Company by the Commission. This would also suggest an ROE in the range of 10.00-10.35% supported by an analysis of its peer group, and which would also recognize the recent upward trend in ROE's approved by other jurisdictions and the significant benefits resulting from Spire's growth, cost management, investments in efficiency, and best practices in serving customers.

i. Return on Common Equity – What is the appropriate return on common equity to be used to determine the rate of return?

Economic Conditions

Most of the parties opposing the Company's request for an ROE of 10.35% commented extensively on the decline in returns on equity over the past decade, but pay little attention to the unchallenged data showing recent growth in the economy, the well-publicized increases in Federal Funds rates, and the increasing authorized rates of return by state regulatory agencies during the last year. Such economic and regulatory trends are contrary to MECG's assertion that capital costs have remained flat to declining. (MECG Brief, p. 20).

In particular, Staff witness David Murray testified that he had reviewed reports that the Federal Reserve Chair Janet Yellen expected to continue to raise interest rates in the future. (Tr. 1298). He also acknowledged that Jerome Powell, President Trump's recent nominee to serve as the new Chairman of the Federal Reserve, also has stated that he intends to continue the trend of raising interest rates. (Id.) Finally, he candidly acknowledged that the stock market consensus at the time of the hearing was that interest rates would be raised in December. (Id.) (They were) Mr. Murray also confirmed that the rate of annual growth in the Gross Domestic Product ("GDP") has increased to in excess of 3 percent since the Commission issued its last decision in the KCP&L rate case. (Tr. 1298-99). Such trends show that the economic conditions are changing and are expected to continue to increase the cost of capital in the upcoming year when new rates are in effect.

MECG also mistakenly argued that "the evidence indicates that the return on equity decisions of state utility commissions are either declining or remaining stable." (MECG Brief p. 25). In fact, the record indicates that in the last half of 2017, the average authorized returns on equity increased to 9.89%. (Tr. 1189; Ex. 40, Ahern Surrebuttal, p. 40) from 9.5% during

the first half of the year. (Ex. 204, Staff Cost of Service Report, p. 40).

Not only are the proposed ranges of Staff (9.0%-9.5%) and OPC/MIEC (8.9%-9.4%) below the national average returns authorized by other state regulatory agencies, they are also below the level of earnings expected by Value Line for the companies in Mr. Murray's Natural Gas Distribution Group for which Value Line publishes a projected return on common equity for the years 2020-2022. As explained in Spire's Initial Brief, the latest (September 1, 2017) Value Line Ratings & Reports (Standard Edition) for the companies in Staff's Natural Gas Proxy Group indicates that Value Line expects the companies in Staff's Natural Gas Proxy Group to earn an average 9.90% return on year-end book common equity over the next 3-5 years. Simply stated, Staff and OPC/MIEC proposed ranges of ROEs are inadequate in comparison to the average authorized returns from other regulatory agencies and the expected return on book common equity of the Natural Gas Proxy Group of 9.90%. Thus, such recommendations are not consistent with the requirements enunciated in the ***Hope*** and ***Bluefield*** decisions. Such low recommended return on common equity ranges should therefore be rejected by the Commission. (Ex. 39, Ahern Rebuttal, p. 40).

The Experts

As to be expected, each of the parties sponsoring ROE witnesses opposed to the Company's recommendation praised the abilities and credentials of their experts. (Staff Brief, pp. 18-19; OPC Brief, p. 7l; MIEC Brief, p. 7). Staff wisely did not mention that Staff witness David Murray believes the actual cost of equity for LAC and MGE "is presently in the range of 6.90% to 7.70%" (Ex. 2043, Staff Cost of Service Report, p. 7), but instead mentioned only in passing that he believes "that the Companies actual cost of common equity is significantly lower that (sic) his recommended range of 9.0% to 9.5%." (Staff Brief, p. 25). Mr. Murray candidly testified at the hearing that "without a doubt" (Tr. 1295) such a low range of 6.9% to 7.7% had

not been found to be reasonable by any state agency for many years as an allowable return. (Tr. 1292).

Several of the parties touted the background and performance of OPC/MIEC witness Michael Gorman as a "credible" and "balanced" witness. (MIEC Brief, p. 7; OPC Brief, p. 7; MECG Brief, p. 10). However, it must be recognized that Mr. Gorman has consistently appeared before this Commission and opposed the ROE proposals of public utilities primarily on behalf of large, blue chip industrial companies. *See e.g.*, *Report And Order*, Re Kansas City Power & Light Company, Case No. ER-2010-0355, p. 112 (April 12, 2011); *Report And Order*, Re: Ameren Missouri, Case No. ER-2012-0166, p. 65 (December 12, 2012); *Report And Order*, Noranda Aluminum v. Union Electric Company, Case No. EC-2014-0223, p. 10 (October 1, 2014). These parties do not name one utility that Mr. Gorman has ever represented and his pre-filed testimony is silent on the issue. (Ex. 407, Gorman Direct, Appendix A.)

ROE Methodologies

Several parties continue to criticize the methodologies used by Ms. Ahern (and vicariously her colleague Mr. Robert Hevert) who conducted several standard analyses – applied several well-recognized cost of common equity models (i.e., the Discounted Cash Flow ("DCF"), the Risk Premium Model ("RPM") and the Capital Asset Pricing Model ("CAPM") to the market data of the Natural Gas Proxy Group as well as a Non-Price Regulated Proxy Group. (Ex. 38, Ahern Direct, pp. 3-45; 9-34). There is no factual basis for such criticism. (Ex. 40, Ahern Surrebuttal, pp. 2-39).

Ms. Ahern has an extensive background and experience throughout the country representing numerous public utilities and municipalities. She has appeared in several Missouri cases on behalf of Ameren Missouri, Missouri Gas Energy, and Missouri-American Water Company over a number of years. (Ex. 38, Ahern Direct, Appendix A, page A-10). Similarly,

Mr. Hevert has an extensive background in rate cases in Missouri and throughout the country. (Ex. 36, Hevert Surrebuttal, Schedule RBH-SR1). Although Mr. Hevert's ROE recommendation was not followed in the recent KCP&L case, it was accepted in the recent Liberty Utilities case. See *Report and Order* at 26-29, In re Liberty Utilities Corp., No. GR-2014-0152 (Dec. 3, 2014) (awarding ROE of 10.0% based on Mr. Hevert's proposed range of 10.0-10.5%).

Flotation Adjustment Should Be Included

Several parties continued to challenge Ms. Ahern's inclusion of a flotation cost adjustment in her analysis. (Staff Brief, p. 20; OPC Brief, p. 10; MIEC Brief, p. 16) Their criticisms are without merit. In particular, Staff incorrectly argued that Ms. Ahern's flotation cost adjustment violates Spire Missouri's Stipulation and Agreement in Case No. GM-2013-0254. (Staff Brief, p. 20). The Stipulation in that case stated:

> Laclede Gas including its MGE division shall not ever seek to directly or indirectly include or recover in any future proceeding any transaction costs, which as defined herein include, but are not limited to, outside service costs relating to gaining regulatory approval, development of transaction documents, investment banking costs, and costs related to raising equity incurred prior to closing of the Transaction." (Stipulation and Agreement, p. 9, Case No. GM-2013-0254.)(emphasis added).

Ms. Ahern's flotation cost adjustment is not an effort to recover costs related to raising equity incurred prior to the closing of the MGE transaction. Instead, it is simply an adjustment needed to recognize that the return on equity required by stockholders must reflect the fact that there are flotation costs associated with any issuance of common equity. This adjustment is prospective, and does not retroactively recover previous costs associated with raising equity related to the MGE acquisition.

Regardless of the reasons for Spire's issuance of common stock, the fact remains that the Company's shareholders are entitled to receive recovery of its flotation costs just as Spire

Missouri is entitled to receive recovery of debt issuance expenses since there is no other mechanism in the ratemaking paradigm with which such costs can be recovered. (Ex. 40, Ahern Surrebuttal, p. 18).

Business Risk Adjustment Should Be Included

Staff, MECG and MIEC argued that the Company's service agreement with Spire Inc. mitigates LAC/MGE's stand-alone small company risk. (Staff Brief, p. 21; MECG Brief, p. 24-25; MIEC Brief, p. 16). These parties are incorrect that the service agreement mitigates Laclede/MGE's stand-alone investment risk. As explained by Ms. Ahern, the stand-alone investment risk of the Company is not mitigated by the service agreement. Rather, it is the effect of the Company's stand-alone investment risk on ratepayers which is mitigated through lower costs passed on through rates that are lower than they otherwise would be. If the Companies were stand-alone entities without such an agreement, their collective investment risk would remain the same, as the collective risk of their respective operations and rate bases would be the same, but the associated costs would be higher. Hence, it is the effect of the Company's greater investment risk due to their small collective size relative to the proxy groups, and not their collective investment risk itself, which is mitigated. (Ex. 40, Ahern Surrebuttal, p. 26). The arguments of Staff, MECG and MIEC on this point should be rejected.

Finally, there is the issue of whether the Company's ROE should be adjusted if the Commission adopts the Company's proposed RSM or the weather normalization rider adjustment proposed by Staff. Both parties have suggested in their initial brief that a 10 basis point adjustment would be appropriate. Because many of the peer utility companies used to derive the various ROE's recommended by the parties in these cases already operate under similar mechanisms (Tr. 1151), such an adjustment is already "baked" into such ROE recommendations. Accordingly, it would be more appropriate to adjust the ROE upward if the

Commission does not approve an RSM.

Under no circumstances, however, should the Commission impose a downward ROE adjustment in connection with Staff's proposed Weather Normalization Adjustment Rider ("WNAR"). As the Company's explains elsewhere in this reply brief, without the revisions proposed by the Company, the WNAR would provide the Company and its customers with significantly less protection from the vagaries of weather than is currently provided by the existing rate design. Accordingly, the WNAR proposed by Staff should not be adopted at all without such revisions, and no ROE adjustment, other than an upward one, would be warranted if such revisions were not made. The same is true if the Commission were to radically alter its ratemaking practices by adopting some of the other extreme proposals in this case. These include, among others, the proposal by Staff and OPC to provide a 1.5% return on storage inventories, OPC's proposal to break decades of regulatory precedent and apply a long-term debt rather than overall capital cost return to the Company's pension assets, and Staff's and OPC's proposals to adopt hypothetical capital structures that bear no relationship to the actual capital structure being used by the Company. The best course of action would be for the Commission to simply reject these unjustified proposals, and the Company strongly recommends that it do so. But failing that, the Company believes that the Commission has an obligation to view how its decisions and policies may be affecting the Company's risk, through a larger lens that goes beyond the single issue of customer usage and revenue effects.

In summary, the Commission should adopt the Company's recommended return on equity of 10.00-10.35% which is clearly within the zone of reasonableness, given the national average authorized returns of 9.89%. As explained by Ms. Ahern, this ROE authorization is appropriate for purposes of this case and meets the tests of ***Hope*** and ***Bluefield***. As suggested by Staff witness David Murray, as a frame of reference, the Commission use the 10.224% pre-

tax ROR that was deemed reasonable for protecting ratepayers in both the MGE acquisition case and the most recent MGE rate case as a starting point for determining both ROE and capital structure in this case. By using this reference point, the Commission can see that the ROE recommendations of Staff and OPC/MIEC should be rejected as creating unreasonably low pre-tax costs of capital when viewed in conjunction with their recommended capitalizations. These ROE's are really asking for returns far below that 10.224% reference point for Staff of 8.745-9.119% (or 7.170-7.770% using their original analysis of 6.90-7.70% ROE) and 9.110-9.499% for OPC. Meanwhile, the Company's range of 10.00-10.35% results in a pre-tax return of 10.685-10.993%. less than 50 basis points above the 10.224%.

ii. Capital Structure: What capital structure should be used to determine the rate of return?

As discussed in the opening section of the Cost of Capital issue, the Company believes the unreasonableness of the capital structure recommendations of the Staff and OPC/MIEC are graphically illustrated by the ROR they produced compared to the ROR that was deemed reasonable for the Company in the MGE Acquisition proceeding, Case No. GM-2013-0254, and the subsequent MGE rate case proceeding, Case No. GR-2014-0007. And, as discussed below, they have presented nothing in their Initial Briefs that would dispel this conclusion.

In their capital structure recommendations, Staff, OPC, MIEC and MECG have proposed to arbitrarily reduce the equity component of the Company's capital structure well below its actual equity component of 54.2%. (Staff Brief, pp. 26-29; OPC Brief, pp. 11-13; MIEC Brief, pp. 17-19; MECG Brief, pp. 38-41). These inappropriate proposals would not allow the Company to recover the actual costs of the capital it has invested in the utility. As explained in the Company's initial brief, these proposals attempt to inappropriately use the Company's acquisition activities to impose an artificially low equity component substantially

below the equity level traditionally used by the Company and approved by the Commission for years prior to these acquisitions. They are also significantly below the average equity component reflected in the capital structure of the Company's peer utilities.

The competent and substantial evidence demonstrated that four of the natural gas companies (Atmos Energy, Northwest Natural Gas, Southwest Gas, OneGas, and Spire Inc.) in Staff's proxy group had five-year average common equity ratios of 53.73%, 53.34%, 48.85%, and 53.53%, respectively. (Ex. 38, Ahern Direct, Schedule PMA-D2, page 2 of 2). In contrast, the capital structures recommended by Staff and OPC/MIEC contain equity components of 45.56% and 47.20%, respectively, substantially lower than the Company's peer group.

Similarly, Ms. Ahern's seven natural gas proxy companies had common equity ratios which averaged 55.01%, with a median of 53.39%, for the year 2015. (Ex. 39, Ahern Rebuttal, p. 9 and Schedule PMA-D2). The five-year average common equity ratio for Ms. Ahern's proxy group ranged from 53.46% in 2014 to 57.52% during the period of 2011-2015. (Ex. 38, Ahern Direct, Schedule PMA-D2). Like Staff's proxy group, Ms. Ahern's natural gas proxy group also had five-year average common equity ratios substantially above the common equity ratios proposed by Staff, OPC/MIEC, and MECG in this case.

Even Public Counsel cited evidence that the average capital structure used for ratemaking purposes over the last 17 years has consisted of 51.05%, again substantially above the 47.20% that Public Counsel is recommending in this proceeding. (Public Counsel Brief, p. 12). Similarly, MECG pointed to evidence that "the equity ratio for ratemaking purposes has fluctuated between 50.33% and 51.99%" (MECG Brief, p. 31)--again much higher than what MECG is recommending in this case.

Staff and MECG also raised an erroneous argument that the use of Spire Missouri's actual capital structure for ratemaking violated the terms of a stipulation and agreement in Case

No. GM-2013-0254. (Staff Brief, pp. 28-29; MECG Brief, pp. 33-35). The Stipulation and Agreement in Case No. GM-2013-0254, pp. 8-9 contained the following provision:

> 3. PREMIUM AND ACQUISITION COSTS
>
> a. Premium. The acquisition premium is the total purchase price above net book value. The amount of any acquisition premium paid for MGE in connection with the Transaction shall not be recovered in retail distribution rates. Nothing herein shall preclude any party to this Agreement from taking a position in any future ratemaking proceedings involving the Laclede or MGE Divisions in Missouri regarding the ratemaking measures and adjustments necessary to ensure no impact from the acquisition premium on rates. Neither Laclede Gas nor its MGE division shall seek either direct or indirect rate recovery or recognition of any acquisition premium in any future general ratemaking proceeding in Missouri

In this case, the Company is not seeking any amount of the acquisition premium paid for MGE, and has specifically excluded the acquisition premium from its proposed cost of service in these cases. (Ex. 36, p. 5, lines 2-5) It is ludicrous to suggest that by proposing a 54.20% common equity ratio and a 45.80% long-term debt ratio, the actual ratios on Spire Missouri's books, that the Company is attempting to recover any acquisition premium. The fact that the Company used both debt and equity to acquire MGE has no bearing on the recovery of (or lack of recovery) of an acquisition premium.

As explained herein, it is the parties that are suggesting that the Commission "remove" goodwill from the capital structure of the Company to reflect the acquisition of MGE that are attempting to use the MGE transaction as a basis for affecting the rates of the Company's customers. Such erroneous arguments by Staff and MECG should be given no countenance at all, and the Commission should soundly reject them.

Public Counsel, MIEC, and MECG proposed to utilize the actual stand-alone capital structure of Spire Missouri as of September 30, 2017, with removal of approximately $210 million of "equity". (OPC Brief, pp. 11-13; MIEC Brief, pp. 17-19; MECG Brief, pp. 32-34)

For the reasons stated herein, the Commission should reject these proposals.

With their proposed "goodwill adjustment," Public Counsel, MIEC and MECG are recommending a capital structure that is inappropriate, unreasonable, and in Mr. Gorman's words, "light on common equity" (Tr. 1376) and "has a relatively thin amount of common equity." (Tr. 1375).

MECG argues that the "inclusion of goodwill as equity in the capital structure constitutes bad ratemaking policy." (MECG Brief, pp. 35-38). However, this argument should be rejected. MECG did not dispute the fact that the acquisition of MGE by Laclede Gas was not financed by only common equity. In reality, LAC's purchase of MGE's assets, both tangible and intangible (goodwill), was financed by a mix of debt and equity. The synergies or savings produced by the acquisition of MGE were produced because MGE, as a whole, was purchased by Laclede. Laclede would not have been able to produce those synergies if it had not purchased all of the assets of MGE, including the goodwill, and paid a reasonable acquisition premium. Since it is not possible to trace specific portions of the acquisition financing to specific assets, including goodwill, it is inappropriate to suggest that the goodwill was financed by common equity alone. (Ex. 36, Hevert Rebuttal, p. 7).

As explained in Spire's initial brief, an equity investor commits funds based upon the expectation of earning a compensatory return derived from all assets (tangible and intangible) owned by the subject company. Any successful capital offering, whether it is debt, equity or both, depends on the profitability and cash flow generated by the entire enterprise. That was the case in the MGE transaction, for which capital was raised in excess of the book value of MGE's tangible assets, giving rise to the approximately $210 million goodwill balance. (Id. at 9-10).

At pages 37-38 of its Initial Brief, MECG also cites a number of utility commission

decisions from a variety of states in which a commission supposedly excluded "goodwill" from the capital structure. Assuming MECG has compiled an exhaustive list, its tabulation of these decisions would suggest that the vast majority of states have either not considered or have rejected making this kind of adjustment. But even a number of the decisions cited by MECG are either inapposite or do not support MECG's proposition. For example, nearly a third of the decisions cited by MECG involve utilities operating in Illinois. What MECG fails to disclose is that the treatment of goodwill in Illinois is part and parcel of a "formula ratemaking" framework that was approved by the Illinois legislature a number of years ago. As discussed in one of the cases cited by MECG, that formula ratemaking framework has a variety of features that MECG would never find in a regulatory proceeding or endorse using in Missouri. As summarized in ***Ameren Illinois Company d/b/a Ameren Illinois,*** 2013 WL 6576487, p. 3 (Ill.C.C. December 9, 2013), this framework includes the following features:

> The revisions to the Act made by Public Acts 97-0616, 97-0646, and 98-0015 provide that an electric utility that commits to undertake an infrastructure investment program pursuant to Section 16-108.5(b) may elect to recover its delivery services costs through a performance based rate approved by the Commission. The performance based rate tariff (for AIC, Rate MAP-P) sets forth a formula for calculating a delivery service revenue requirement that will be used to set delivery service charges for retail electric customers. The formula includes the specific cost components that form the basis of the rates charged to the utility's delivery service customer classes. The performance based rate provides for recovery of a utility's actual, prudently incurred and reasonable costs of electric delivery services, except for those costs that the utility continues to recover through automatic adjustment clause tariffs. The performance based rate also reflects the utility's actual capital structure for the applicable year (excluding goodwill) and includes a cost of equity, the calculation of which is addressed in Section 16-108.5. The performance based rate is intended to operate in a standardized and transparent manner and be updated annually to reflect (i) historical data from the most recently filed FERC Form 1, plus projected plant additions and correspondingly updated depreciation reserve and depreciation expense for the year of filing, (ii) a reconciliation of the revenue requirement reflected in rates for each year, with what the revenue requirement would have been had the actual cost information for the year been available at the filing date, and (iii) any adjustments, including adjustments to reflect an earned rate of return on

common equity outside the statutory range, required by Section 16-108.5(c).

MECG cannot even bring itself to support an RSM mechanism that doesn't even affect its client, and yet it selectively cites this one goodwill feature of a formula ratemaking process that it undoubtedly abhors. All of which demonstrates the pitfalls of simply citing decisions without providing any context regarding the reasoning behind them or other critical elements of the ratemaking process in the particular state issuing the decision that may differ markedly from Missouri's and make such a decision inapplicable.

The Kansas Corporation Commission's July 21, 2001 ***Westar*** decision cited by MECG is another example. That decision did not even consider whether goodwill should be subtracted from the utility's equity component, let alone determine that it should be. Perhaps MECG was confused because the KCC did exclude certain costs relating to goodwill *advertising*. In any event, this decision, like so many others cited by MECG, does not support the proposition for which it is cited.

OPC/MIEC's approach not only ignores the benefits accruing to customers from those synergies, it also penalizes the investors whose capital enabled those benefits in the first place. Again, OPC/MIEC's proposed "goodwill" adjustment is inappropriately one-sided. Laclede actually financed the acquisition of MGE with more debt than equity, which means the equity ratio used for rate base actually dropped because of the financing of the assets, including goodwill. (Id. at 6) The rate base, which includes no goodwill, in combination with the capitalization ratios of the utility create the capitalization utilized for determining revenue requirement for ratemaking purposes. It therefore makes no sense to exclude goodwill as an assumed 100% equity component when the transaction was financed with a mix of both debt and equity, the capitalization after the financing included a lower equity component than prior to the transaction and the rate base was not increased whatsoever to include the goodwill.

For these reasons, the Company respectfully requests that the Commission reject OPC/MIEC's proposed "goodwill adjustment" and instead utilize the actual capital structure of Spire Missouri in this proceeding.

ii. Cost of Debt – What cost of long-term debt should be used to determine the rate of return?

The Company's actual cost of debt was updated from 4.159% (Ex. 38, Ahern Direct, Schedule PMA-D1 to 4.123% (Ex. 68, Noack True-up Direct, Scheduled F) and it should be utilized in connection with Spire Missouri's actual capital structure. Contrary to the assertions of Staff that Spire Inc.'s consolidated embedded cost of long-term debt should be utilized (Staff Brief, p. 29), the Commission should utilize the Company's actual stand-alone capital structure, including its actual embedded cost of debt, based upon Spire Missouri's actual capital structure.

iii. **Should short-term debt be included in the capital structure? If so, at what cost?**

As explained in the Company's initial brief (Company Brief, pp. 44-47), short-term debt should not be included in the capital structure used for ratemaking in this case. The Company's short-term borrowings are fully utilized to finance its short-term assets that are not included in rate base, so such debt should not be in the Company's permanent capital structure. Short-term debt should not be included in the capital structure because the average level of construction work in progress and other short-term assets (including propane, margin calls on multi-year hedging programs and deferred gas costs subject to the PGA carrying costs) exceeds the average level of short-term debt outstanding during the true-up period after taking into consideration the September 15, 2017 funding of $170 million of long-term debt instruments. (Ex. 22, Buck True-up Direct, p. 2; Tr. 1269-70).

OPC also concurred that "Short-term debt should not be included in the determination of the capital structure." (OPC Brief, p. 23). Not including short-term debt in the capital structure has been the long-standing approach used for decades by the Commission. For example, Staff witness Murray confirmed that the Commission has not included short-term debt in the capital structures of Summit Natural Gas, Liberty Utilities, Kansas City Power and Light Company, and Ameren Missouri. (Tr. 1317-19) Nor did Staff include short-term debt in Laclede's capital structure in the last MGE rate case, Case No. GR-2014-0007. (Tr. 1304; Ex. 60) In fact, Mr. Buck testified that he was unaware of the Staff or Public Counsel or any other party including short-term debt costs in past cases for 15-20 years. (Tr. 1270). The Commission should not depart from this long-standing practice.

Staff's approach, on the other hand, is not consistent with the long-standing practice of the Commission which has included gas inventories in rate base, but rarely included short-term debt in the capital structures of major public utilities. (Tr. 1510-11). Although Staff originally stated in its direct and rebuttal testimony, that LAC's storage inventory costs should be included in base rates to ensure such costs were treated in the same manner as they are for all other Missouri gas utilities, its attempt to apply a short-term debt rate to such inventories would ensure just the opposite. As explained in the Company's initial brief, Ameren, Empire, Liberty and MGE have no short-term debt included in their capital structure, even though all are gas utilities regulated by the Commission and all have gas inventories included in rate base. (Tr. 1435). As a result, adopting Staff's approach would effectively provide LAC and MGE with a 1.5% return on these costs while other LDCs are permitted to earn a full return which includes the cost of common equity and long-term debt. That is not the kind of disparate regulatory treatment that the Commission should approve. There is no reason to change the Commission's policy in this case to include short-term debt in major public utilities' capital structures.

For all of these reasons, the Commission should reject Staff's eleventh hour attempt to change the Commission's practice of excluding short-term debt from the capital structures of major public utilities.

b. Rate Case Expense

i. What is the appropriate amount of rate case expense to include?

Executive Summary: The Commission should approve all prudently incurred rate case expense, especially in a case where the Company was required to file a rate case in order to continue collecting revenues under the ISRS Statute.

Argument: The case at the center of rate case expense issue is a 2015 Commission decision in a KCPL rate case, ER-2014-0370. The case is ***Re: Kansas City Power & Light Company****,* 509 S.W.3d 757 (W.D. Mo. 2016). Staff partially follows *KCPL,* but then diverges from it in a way that completely undermines the rationale behind the Court's approval of the Commission's approach.

At first, Staff appeared to follow the Commission's rate case expense prudence analysis by questioning whether the level of rate case expense in this case is unreasonable and imprudent. (Staff Brief, p. 32) Staff suggests that it is unreasonable and imprudent because rate case expenses have increased significantly over the economical expenses that the Company incurred in prior cases. (*Id*. At pp. 32-33).

According to Staff, this increase was due to the unusually large number of issues raised by the Company and taken to hearing. Staff provides as examples the Company's positions on ROE, capital structure, trackers, revenue stabilization mechanism ("RSM"), performance metrics, and synergies. Staff sees as meaningful the Company's estimate that it controlled roughly half of the issues brought to hearing. (Id., p. 33)

Staff tells only half of the story. First, it should be remembered that this rate case is

actually two rate cases, covering the two largest gas utilities in the state. Second, it is the Staff that drove the cost of capital controversy by inserting short-term debt in the Company's long-term capital structure and advocating a 45.56% equity component for a company with 54.2% equity. It is especially telling when a supposedly neutral party (Staff) chooses a cost of capital below that of the interested parties. Staff's pre-tax rate of return is more than 30 basis points below the return advocated by the consumers and industrial customers. In surrebuttal, Staff repeatedly lauded the 10.224% pre-tax rate of return that MGE has been operating under while at the same time advocating a mid-point return of 8.932%. On issues like capital structure, a 'neutral' party like Staff eliminates the need for adversaries. Regarding rate case expense, it is particularly galling for Staff to take such a threatening position on capital structure and then blame the Company for protecting itself by retaining consultants.

Staff also fails to acknowledge that, unlike the finding in the KCPL case, the issues raised by the Company were not the type of issues designed to boost revenue requirement. The RSM is a non-revenue producing, two-way usage adjustment mechanism that primarily protects customers from overpaying revenues to the Company in cold winters and underpaying them in warm winters. The performance metrics proposal is also a two-way mechanism designed to make the Company more directly accountable for customer service. Staff further failed to note that the Company is pursuing only one tracker, an environmental tracker that is explicitly authorized by the legislature. This tracker is also a reconciling mechanism, intended to permit the company to recover its environmental costs, no more and no less. (Tr. 1709)

Staff's view that half of the issues brought to hearing were Company issues entirely misses the point. The more unique circumstance is that the Company did *not* control half of the issues in its own case. These issues contributed to driving up rate case expense and include, but are not limited to, Surveillance (Staff), School Transportation (MSBA, Staff), Energy

Efficiency and Weatherization (DE, NHT and Spire Missouri), Low-income Program (Consumer's Council and Spire Missouri), PGA/ACA/Pipeline (Environmental Defense Fund), Combined Heat and Power (DE), and Hydrostatic Testing (OPC). (Tr. 1708, 1733-34) In addition, the Forest Park issue arose from a 2014 event and was raised by Staff and OPC. (Tr. 1709, 1732)

Staff chose not to follow the KCPL case by reviewing rate case expenses on a line-by-line basis. Staff's goal was to do a prudence review that first assigned to the Company 100% of the alleged imprudent costs, and then further assigned to the Company a share of the prudent costs. Staff originally asserted several disallowances, but in the end trimmed them down to one: Staff found the Company imprudent for hiring a consultant to perform a cash working capital ("CWC") study when the Company had done the study in-house in the past (Staff Initial Brief p. 34).

In the KCPL case, the Commission declined to get involved in the details of prudence, arguing that it could not determine the prudence of individual expenditures. The Commission instead focused on rate case expenses incurred as a whole in deciding whether KCPL had been in some way imprudent (ER-2014-0370, Report and Order, p. 69).

Staff's tactic completely blows up the Commission's KCPL rationale. As evidenced by the fact that it originally identified several imprudent rate case expenses, and then narrowed them down to one, Staff demonstrated that it can distinguish between prudent and imprudent expenses. It therefore must eliminate only the imprudent rate case expenses, and not disallow the remaining prudently incurred expenses.

With respect to the prudence of the CWC study, the Staff does not question the performance of the study, only that the Company contracted out for it rather than doing it in house. Company witness Buck testified that he had done CWC studies in the past, but given

the fact that we were putting together two rate cases, he simply did not have time to handle that duty. Under these circumstances, there is nothing imprudent about contracting such a study. In fact MGE has always contracted out their CWC studies. (Tr. 1745, l. 12-19) Given the Company's ability to defer these rate cases for four years, Spire Missouri's expenditure was eminently reasonable. As long as the amount spent by the Company was reasonable for the service purchased, it is not Staff's place to dictate how the Company acquires that service.

Finally, Staff cites the KCPL case for the proposition that rate cases benefit shareholders. Spire Missouri was forced to file this rate case as a consumer protection under the ISRS Statute. But for that statute, Spire Missouri was unlikely to have filed the rate case last April 11 (Tr. 478) Given the fact that this case has burdened the Company and diverted its employees from their normal business duties of serving customers, not to mention the costs and risks that parties will take unreasonable and opportunistic positions, Spire Missouri does not see this case as beneficial to the Company or its shareholders. (Tr. 492)

ii. **What is the appropriate normalization period for recovering rate case expense?**

Executive Summary and Argument:

The Company believes three years is an appropriate period to recover rate case expense. The Commission should also take into account frequency of rate cases in determining whether a utility should bear rate case expense. For example, it has been now 4½ years since LAC last completed a general rate case, in which it incurred a record low $80,180 in rate case expense. If the Commission seeks to assess some form of rate case expense to the Company, we suggest lengthening the rate case expense recovery period. At the hearing and in its brief, Staff recommended a four-year recovery period. (Tr. 1763; Staff Brief, p. 31) If the Company is permitted to recover its rate case expense in this case, it would not be opposed to such a recovery period.

d. PGA/ACA Tariff Revisions

i. Should LAC have new PGA/ACA tariff provisions pertaining to costs associated with affiliated pipeline transportation agreements?

Executive Summary and Argument: EDF, the sole proponent in this proceeding of radically altering the current structure of the Company's PGA/ACA tariffs and Standards of Conduct, offers nothing in its Initial Brief to support its proposals that have not already been adequately addressed in the Initial Briefs of the Company and the Staff. (Company Initial Brief, pp. 52-55; Staff's Initial Brief 35-38) As both the Company and Staff have pointed out, the changes proposed by EDF would require fundamental and potentially unworkable changes in the regulatory process that the Commission has long used to review procurement decisions by the gas utilities it regulates.

This is especially true of the Commission's long-held policy preference for reviewing such decisions after the fact for prudence and reasonableness rather than trying to pre-approve them in advance. That this is the exact policy reversal that EDF intends the Commission to make is demonstrated at page 12 of its Initial Brief where EDF acknowledges that once the Company complied with the analytical formula that EDF is recommending the Commission adopt, it "would then be permitted to recover the lesser of: (1) the all-in cost times the design-winter usage of the propane capacity or (2) the all-in cost of the new replacement capacity times the same usage." Of course, all the Commission has to do to accommodate this new vision of how procurement decisions should be evaluated is to step into utility management's shoes and make critical decisions, years in advance of the pipeline's actual completion, on how its cost, reliability, diversity of supply, and other impacts should be assessed and factored into a recovery determination, all based on a few dozen pages of testimony by someone who is largely unfamiliar with the Company, its history and its operational requirements for the

transportation capacity and gas supplies needed to serve its customers efficiently, effectively and reliably. The Company strongly believes that the Commission should decline this unappealing invitation.

It is also clear that the changes being proposed by EDF are not really being sought to protect the Company's customers, as it asserts, but to further its efforts to simply stop a pipeline project, in this case the Spire STL Pipeline project. EDF's pursuit of that objective was reconfirmed by its recent effort to lodge a copy of the transcript and its brief in these cases with the Federal Energy Regulatory Commission ("FERC") in the Spire STL Pipeline proceeding. ***Re: Spire STL Pipeline, LLC,*** CP17-40-000 and CP17-41-000. EDF has also expressed its opposition to the Spire STL Pipeline project in that FERC proceeding – a proceeding in which this Commission is also participating. While EDF may be within its rights to cross-pollinate these two proceedings, such action underscores EDF's true objective in this case – namely to stop the pipeline project in any way it can.

It also raises anew the somewhat troubling issue caused by the Commission being a party to one proceeding while it is also a decision-maker on the same subject matter in another proceeding. As the Company indicated in its opening statement on this issue during the evidentiary hearing, it has always been a strong proponent of the Commission's involvement in FERC proceedings, and actually testified in Committee in favor of legislation that was that was designed to re-establish the Commission's statutory authority to do so. EDF's efforts, however, to try issues relating to the pipeline in both forums at the same time naturally raises questions regarding whether and how any applicable restrictions or notice requirement under the Commission's rules governing ex-parte and extra-record communications are being observed (see 4 CSR 240-4.015 – 4.030) and whether the Commission's decision in these proceedings are being influenced by arguments and materials being submitted outside the

record of such proceedings. The Company certainly does not mean to imply that these concerns are anything other than hypothetical ones, but they can all be avoided by doing what is appropriate in any event, namely rejecting any further consideration of EDF's flawed proposals in these cases.

Finally, it is striking to note that in pursuing its goal of stopping the Spire STL Pipeline, EDF has managed to cast aspersions on the adequacy of the regulatory review process at both the state and federal level. At page 2 of its Initial Brief, EDF opines that the "current regulatory oversight structures [at both the Missouri Commission and FERC] are insufficient in protecting against unreasonable affiliate transportation costs." It is unfortunate enough that EDF has misappropriated the interests of the Company's customers as the pretext for its anti-pipeline agenda. But it is even worse for it to suggest that its efforts and ideas are indispensable because the regulatory process and the regulatory personnel that have long attended to those matters on behalf of customers are simply not up to the task. The Company would respectfully submit nothing has been presented in this proceeding that would warrant such an elevated self-appraisal of EDF's contribution to the regulatory process and that its proposed changes to the Company's ACA/PGA tariffs and Standards of Conduct should be rejected by the Commission.

e. CAM

i. Should a working group be created following this rate case to explore ideas for modifying the LAC and MGE CAM?

Executive Summary and Argument: For the reasons set for in its initial brief, the Company continues to believe that a working group is the preferred and most sensible vehicle for exploring how the Company's Cost Allocation Manual ("CAM") might be updated to ensure that shared corporate support services and other costs are properly charged and

allocated among Spire's Missouri utilities and its other regulated and unregulated businesses. The Staff indicated in its brief that it would be happy to participate in such a process (Staff Initial Brief, p 41.) And while OPC said it would not wish to participate immediately, the Company is hopeful it would alter its position if the Commission rejects, as the Company believes it should, OPC's poorly supported and unnecessary proposal to hire yet another outside consultant.

For the reasons discussed in its Initial Brief, the Company believes that these collaborations among the parties who know the Company, the regulatory environment in Missouri, and each other, have been successful in the past in not only developing the current CAM but also in addressing various issues that have flowed from it. (Spire Missouri Brief, p. 56) There is no reason to believe that such efforts could not be equally successful in the future and they should certainly be tried before additional costs are incurred to hire yet another outside consultant.

ii. Should an independent third-party external audit be conducted of all cost allocations and all affiliate transactions, including those resulting from Spire's acquisitions, to ensure compliance with the Commission's Affiliate Transactions Rule, 4 CSR 240-20.015?

Executive Summary and Argument: There is simply no justification for incurring the significant expense that would be required to hire an independent, third-party consultant to evaluate how the Company and its parent, Spire, are allocating costs among various affiliates and otherwise complying with the Commission's Affiliate Transactions Rules. In suggesting that there is, OPC primarily relies in its Initial Brief on the litany of complaints expressed by the "independent" third-party consultant that it just spent ratepayer money on to presumably undertake this very same exercise in these cases. (OPC Initial Brief, pp. 20-21).

As noted in the Company's initial brief, this is the same consultant that, after reviewing

the allocations of the Company and Spire for a number of months, proposed only two actual adjustments. The first related to her misguided and completely unsupported allocation of approximately $36 million of the Company's newBlue information management system costs to Alagasco and EnergySouth. (Ex. 400, p. 44, line 9, to page 46, line 11). She made this recommendation, even though it was apparent to Staff from the outset that neither Alagasco nor the EnergySouth utilities utilized that system in their operations. (Staff's Cost of Service Report, Ex. 205, p. 120). And she maintained her allocation recommendation even after this basic fact was established with even greater clarity in the rebuttal testimony by the Spire's Vice President in charge of the Company's information technology. (Ex. 32). It was not until the day after she testified, however, that OPC finally withdrew its proposed adjustment that never should have been made in the first place.

As discussed in the following subsection, the only other adjustment OPC's outside consultant proposed relating to allocations is the equally misguided one in which she proposed to adjust the Company's 2016 test year expenses to reflect reductions in shared service costs that have already been reflected in the true-up results submitted by the Company – in other words a classic double dip. The fact that OPC's third party consultant was unable, after months of auditing the Company, to identify any valid adjustments to how the Company and Spire allocated costs during the test year, hardly supports OPC's contention that yet another audit is needed. To the contrary, it strongly suggests that it isn't. Moreover, the fact that the adjustments identified by the outside consultant were so flawed that one had to be withdrawn and the other is ripe for rejection by the Commission raises the issue of why another outside consultant would be hired in the first place to conduct such an audit, assuming there was actually a need for one.

There is also the issue of the cost of hiring such a third party consultant. During the

evidentiary hearing in this case, OPC witness Marke suggested that the Commission simply require that Company pay the first $500,000 in expenses for such a third party consultant, and then half of any amount in excess of that figure. (Tr. 1981, lines 11-16) The Company fully understands that OPC has managed to use its leverage in the current merger proceeding involving Great Plains Energy and Westar to extract a voluntary agreement by that utility to pay such amounts as the price of obtain a Stipulation recommending approval. But that is a voluntarily agreement, and the Company respectfully submits that it would be legally impermissible for the Commission to order such a result. In fact, it smacks of a penalty that OPC is seeking to impose on the Company without proving any violation of law and without following the normal complaint process mandated by law. See Section 386.390.

Even if it were not impermissible to impose such an obligation on the Company, the amount being proposed by OPC for such an endeavor is wildly excessive. In fact, it is nearly 36% of all of the rate expenditures made by the Company for outside legal and technical resources to address a wide variety of issues in this case, ranging from ROE and capital structure to allocations, rate design, pensions and cash working capital. And yet OPC would have the Commission believe that such an amount is necessary to address this one issue?

With all due respect, the Commission has a relatively large Staff and OPC's budget has grown to the point where it was able to contract with multiple outside consultants in this case. There is simply no reason to believe that OPC and Staff do not have the capacity to undertake whatever effort may be necessary or advisable to address this matter. For all of these reasons, OPC's proposal should be rejected.

iii. How should the Commission account for shared services?

The Company did not believe that the OPC would continue to pursue this issue given the evidence that was placed on the record in these cases, but it has. Based on the advice of

its consultant, Ms. Ara Azad, OPC is proposing that the Commission make discrete adjustments to the 2016 test expenses of LAC and MGE of $2.1 million and $922,000, respectively, to reflect the downward trend in shared services cost being allocated to Spire Missouri. (OPC Initial Brief, p. 23). This downward trend in shared service allocations, which totaled over $3 million, however, have already been captured in the true-up of the test year that ended September 30, 2017. (Ex. 8). As a result, OPC is either double dipping and attempting to catch this savings twice or it is proposing to go beyond the update period and recognize savings that have not yet occurred. While there may be certain circumstances where recognizing revenues or costs beyond the true-up period is allowable, this is clearly not one of them given the duplicative nature of OPC's proposed adjustment.

f. Gas Inventory Carrying Charges

i. Should LAC's natural gas and propane inventory carrying costs be recovered through rate base inclusion, as currently is the case with MGE, or recovered through the PGA/ACA process?

Executive Summary: LAC's gas storage costs should be moved back into rate base, an action that would bring LAC in line with MGE and every other gas LDC in Missouri. Moreover, LAC should, like every other Missouri gas utility, be permitted to earn its overall cost of capital on such inventories, consistent with the Commission's historical practice, rather than have a short-term cost of debt applied to these assets. Both Staff and OPC have previously argued against including gas supply inventory carrying costs in the PGA; however, OPC has since reversed its position, and more recently Staff has determined that if gas inventories are to be included in rate base, they should be tied to inclusion of even a larger amount short-term debt in the capital structure, even if it cannot be shown the Company relied upon short-term debt to finance its rate base, including storage.

Argument: As discussed in the Introduction and the Cost of Capital section, this

simple issue represents one of the least respectable actions by the Staff. As part of an overall theme in these cases of integrating LAC and MGE and promoting consistency between them, LAC proposed moving its gas storage inventory back into rate base, as is the case with all of the other gas utilities in the state. Because it anticipated using propane only for a short period of time after the rate case, LAC chose not to include that asset in rate base although the timing difference would likely have worked in the Company's favor.

Staff noted that, in addition to MGE's gas storage inventories being in rate base, "all other Missouri LDCs have used the 'rate base' approach to recover carrying costs associated with gas inventory in their Missouri jurisdictions" (Ex. 205, Staff Cost of Service ("COS") Report, p. 63). MGE, Ameren, Liberty, and Empire all have storage inventory in rate base. Including LAC's storage inventory in rate base merely aligns LAC with MGE and the rest of the Missouri gas utilities and would be the right policy decision. It would also provide the Company with a more consistent and less complicated way to account for these costs since the Company would be able to administer storage inventories in one manner instead of applying two different ratemaking treatments. (Id.)

In rebuttal testimony, Staff witness Sommerer again agreed with the LAC/MGE position, as a matter of consistency among utilities. (Ex. 227, p. 5; Tr. 1428) In surrebuttal, Laclede acknowledged Staff's agreement with the Company's position and welcomed Staff's willingness to treat LAC on par with the other utilities, and to act in accord with Staff's longstanding policy of excluding gas-related costs, such as the gas cost portion of bad debt and gas inventory carrying costs, from the PGA. (Ex. 18, p. 2)

Separate and independent of these gas-related issues, Staff witness David Murray was headed in a different direction, adding short-term debt to the Company's capital structure in order to reduce its equity by 864 basis points (8.64%).

Suddenly, in surrebuttal, Staff witness Sommerer veered into a completely different position, claiming that the movement of gas storage inventory into rate base was tied to having short-term debt in the capital structure. (Ex. 259, p. 3) This single act not only discriminated against LAC compared to the other Missouri gas utilities but did so just two weeks before the hearing. It is inexplicable for a neutral party to take an action such as this in surrebuttal.

Tying gas inventory in rate base to short-term debt in the capital structure is intellectually dishonest. The two are independent of each other. Whether short-term debt should be in the permanent capital structure is a function of whether the company generally has short-term debt that simply meets borrowing requirements outside of rate base, such as Construction Work in Progress. While the balance may increase for periods of time until sufficient borrowing requirements justify a long-term debt issuance, that balance after refinancing should be aligned with those short-term non-rate base requirements, which is exactly what Company witness Glenn Buck's analysis showed. (Ex. 20, sch. GWB-R1) If so, then under the matching principle, short-term debt should be matched with these non-rate base financing needs, and there should be no short-term debt in the permanent capital structure, regardless of how gas storage inventories are financed. It is also readily apparent from a review of the components of this inventory cost that there is not much variability, with two significant elements hardly changing at all due to design and reliability requirements of LAC's Lange storage field. The majority of the costs are constant year-after-year, and consistent with other inventory treatment in rate base such as Materials and Supplies, the amount is based on a 13-month average to mitigate the impacts of any seasonality.

In its brief, OPC laments that placing approximately $80 million in gas inventories in rate base will result in substantial harm to LAC customers and a windfall to LAC shareholders

in the sum of about $8 million. (OPC Brief, pp. 27-28) This is incorrect for three reasons. First, it is the LAC customers who have been receiving this unusual benefit for years while other utilities have appropriately included gas storage inventory in rate base as part of their Commission-approved rates. Second, LAC's PGA already includes over $4 million in gas inventory carrying costs, so this difference is significantly smaller than their estimate. Finally, the move of $80 million in gas storage inventories to rate base is more than offset by the Company's shrewd tax positions that have reduced rate base by $100 million.

Staff's brief points out that MGE had short-term debt in its capital structure in its 2010 rate case. (Staff Brief, p. 42) Staff does not point out that MGE was owned by SUG at the time, which had a highly leveraged capital structure, or that the short-term debt rate was 5.92%, almost as high as the long-term rate. It should also be noted that gas storage inventories were neither tied to the short-term debt, nor even mentioned anywhere in the capital structure discussion of the 2010 rate case order. (Ex. 271, pp. 11-20)

LAC should be allowed to include its gas storage inventory in rate base independent of whether short-term debt is in the permanent capital structure. This would align LAC with MGE and all other gas utilities in Missouri.

ii. Should Line of Credit (LOC) fees be removed from LAC's PGA consistent with inventory inclusion in rate base?

Yes. Consistent with moving the recovering of storage inventory carrying costs from the PGA to base rates, the Company continues to believe that recovery of approximately $4.1 million of carrying costs and associated line of credit fees currently included in the PGA mechanism for Gas Inventory Carrying Cost should also be removed

h. Credit Card Processing Fees

i. Should an amount be included in LAC's base rates to account for fees incurred

when customers pay by credit card, in the same manner fees are currently included in MGE's base rates?

In the Staff's Initial Post-Hearing Brief ("Staff Brief"), Staff opens its discussion of the first sub-issue by stating: "The Company and Staff are in agreement that it is proper to include an amount in base rates to account for credit card fees." (Staff Brief, p. 45). As fully reflected in the record of this proceeding, Staff notes that "Pursuant to the Stipulation and Agreement in Case No. GR-2009-0355, MGE has been including these fees in its rates since 2010. (Footnote omitted). Including the fees for LAC would align Spire's two divisions." (*Id.*).

The only other party addressing this issue is the Office of the Public Counsel ("OPC") who, as Staff notes, continues to erroneously argue that this practice is discriminatory and unfair to customers. Staff devotes two pages of its Brief directly rebutting the misdirected advocacy of OPC, noting that "[t]he facts surrounding this proposal show that it does not constitute discriminatory ratemaking because the option of using a credit or debit card to pay a gas bill will be open to all of Spire's customers if the Commission approves this request. Nothing in the statutes prohibits costs being socialized which benefit all customers." (*Id.*). Indeed, Staff highlights this Commission's precedential Report and Order in MGE's Case No. GE-2008-0352, wherein the Commission "determined that it was proper to grant a variance from several Commission rule provisions to permit MGE to offer electronic billing because, 'customer choices are increased, and both MGE and its customers may enjoy savings from the elimination of paper bills, checks, envelopes and postage stamps;' (footnote omitted) signifying the Commission's recognition of the value of diversifying a customer's payment options and the costs associated with non-electronic forms of payment." (Staff Brief, pp. 45-46).

Staff also addresses OPC's allegation that a "small" number of LAC customers utilize credit cards, by noting: "however, this is based on current practices which charge the customer

the additional fee at the time of the transaction." (*Id.*, p. 46). Staff then reviews the historical considerations resulting in increased customer participation from prior cases (KCP&L, Case No. ER-2016-0285; MGE, Case No. GR-2014-0007), concluding that "[t]his indicates that customers are more likely to use the option of paying by credit card after the removal of the fee at the time of the transaction." (*Id.*).

OPC's argument strains credulity when it cites Staff Director Natelle Dietrich's testimony (on a different issue) to ostensibly support its position here. At pages 28-29 of its Initial Brief, OPC states as follows:

> In her rebuttal testimony in this case, Staff witness Ms. Dietrich noted that "Staff Counsel . . . advises that . . . Missouri law forbids the preferential subsidization of certain ratepayers at the expense of all other ratepayers; therefore, it would be unlawfully discriminatory and preferential to require all ratepayers to subsidize" (footnote 115) the minority of customers who use credit cards to pay their utility bills.

(Footnote 115: Ex. 213, Staff witness Natelle Dietrich, Rebuttal Testimony, p. 3: 8-12). The Commission should be aware that Ms. Dietrich's Rebuttal Testimony identifies the issue being addressed therein as the Division of Energy's ("DE") proposal for compensation in administering LAC's weatherization program. In fact, Ms. Dietrich was responding to the Question: "Does Staff support DE's request for an annual administration fee of up to five percent of LAC's program budget?" Her answer at the referenced lines 8-12 reads as follows: "Based on my conversations with Staff Counsel *related to this request*, Staff Counsel advises that DE's request is unlawful. First, according to Staff Counsel, Missouri law forbids the preferential subsidization of certain ratepayers at the expense of all other ratepayers; therefore, it would be unlawfully discriminatory and preferential to require all ratepayers to subsidize *the administration and delivery of weatherization services.*" (Emphasis added).

ii. If yes, what amount should be included for such fees?

Regarding the appropriate amount to include in LAC's base rates for credit card fees, in its Initial Brief the Company discussed its disagreement with Staff on the appropriate amount to use in the cost of service. Company expert witness Noack, recognizing that there would likely be a ramping up of the number of credit card payments over time, proposed a level that reflects an averaging of anticipated four year amounts. Staff, on the other hand, advocates that the only amount that should be put in rates is based on current usage as of the 12 months ending 9/30/17. As a result, Staff would have the Commission believe that not a single additional transaction would be known and measurable, despite the fact that LAC is adopting the same policy as MGE. Staff has assumed the volume discount rate that MGE experienced for its increased transactions, and Staff's own conclusion that "customers are more likely to use the option of paying by credit card after the removal of the fee at the time of the transaction." According to the testimony, the one fact that is most known and measurable is that the number of transactions will not stay the same. The Company respectfully submits that Staff's proposed cost level is understated and the Commission should adopt Company witness Noack's four-year average adjustment amount of $1,246,619. (Corrected during evidentiary hearing at Tr. 1020; Ex. 30, p. 5, Surrebuttal Schedule MRN-S1). Additionally, OPC's proposal to lower the Company's ROE if credit card fees are included in rates (page 7) is a blatant attempt to zero out any cost recovery for this added service for customers, if not punish the Company, as a reduction in ROE could easily overwhelm these modest costs.

i. Trackers

i. Should LAC and MGE be permitted to implement an environmental tracker?

Executive Summary: Yes. Section 386.266.2 RSMo authorizes the Commission to approve adjustment mechanisms that permit electric, gas and water utilities to recover increases and decreases in their prudently incurred costs to comply with any federal, state, or local

environmental law, regulation, or rule. The Commission has also previously permitted the Company to defer and recover in subsequent rate cases certain environmental remediation costs associated with the Company's former manufactured gas plant sites. The environmental tracking mechanism being proposed by the Company in this proceeding reflects a sensible blend of these two sources of authority for dealing with environmental compliance costs and should be approved by the Commission.

Argument: As expected, Staff OPC and MIEC all opposed the Company's proposed environmental trackers, and all for the same reasons, which are the usual reasons for rejecting tracker requests. (Staff Brief, pp. 48-52; OPC Brief, p. 30; MIEC Brief, pp. 22-23) These parties did not take into account two important factors that make this tracker request different.

First, the Company's request is very narrow – it not only applies to environmental costs, an area that has already been established as the subject of past trackers and statutory authority for current and future adjustment mechanisms (See 386.266.2 RSMo.), but it seeks to track and recover just those specific remediation costs associated with the former manufactured gas plants owned, or previously owned, by MGE and LAC.[2] Second, in addition to being very narrow, environmental costs for these sites tend to be completely unpredictable in cost and timing. The applicable governmental entity may study a remediation plan for years, and then one day send a notice that the plan is approved and work can begin. In other words, the Company may say it is expecting costs to begin this year and ramp up next year, but it is not actually in control of when such costs are incurred. They could be sooner or later than estimated. The one thing the Company does know is that it has 19 of these plants, some of which may need remediation in the next few years, and that remediation could become expensive. (Ex. 8, pp. 21-22) Because

[2] The Company would, of course, continue to pursue reimbursement for such costs from insurers and potentially responsible third parties and offset any deferred costs by such amounts. (Ex. 8, p. 22, lines 10-12).

the Company must apply for an environmental tracker as part of a rate case under the statutory requirements of 386.266.2 RSMo., the Company is requesting the environmental tracker in this case.

The opposing parties correctly point out that there have been no appreciable environmental costs to date and the Company cannot establish when such costs will occur. That is precisely the point. If the Company had control over the matter, it could determine when the tracker would be needed.

A final point that has not been mentioned is that if no environmental costs are incurred, then there will be no costs to track. If the Commission approves an environmental tracker and there are no costs, no one is harmed. If the Commission approves an environmental tracker and there are substantial net costs, the Company will be prepared with a legally authorized mechanism. Either way, the tracker can be revisited in the Company's next rate case. The Commission should consider approving a tracker for a cost that has in the past proven to be substantive, is known to be unpredictable, and is approved for adjustment by the legislature.

j. Surveillance

i. Should LAC and MGE provide surveillance data to the Commission?

Executive Summary and Argument: The Company has reached an agreement with both Staff and OPC on this issue, under which it would provide both parties with certain surveillance reporting on a quarterly basis. The Company has also agreed to provide its general ledger and CC&B subledger data in a secure format on an annual basis between 45 and 60 days after the end of its fiscal year. Staff's brief on this point should refer to this 45-60 day period, rather than 30 days. (Staff Brief, p. 53; Tr. Vol 18, pp. 1551-52, 1569) Accordingly, the only remaining dispute on this issue centers on the request of large volume customer representatives to also obtain the quarterly surveillance information.

With respect to transparency, Spire Missouri has agreed to provide surveillance information to both governmental entities involved in its state regulation, Staff and OPC, and in the format requested by Staff. OPC acknowledged the Company's cooperation on this issue. (Tr. 1552-53)

For the reasons stated in its initial brief, Spire Missouri opposes providing surveillance reports containing non-public data to independent non-governmental corporate entities outside of a rate case. This is especially true if it is not clear who will see the data and whether they can be held responsible for violating confidentiality provisions and securities laws.

MIEC addressed this issue in its brief, but did not respond to the issue of who the MIEC consists of, who would be looking at the information, and who would be agreeing to keep non-public data confidential. Holding the MIEC itself responsible is no comfort, because it appears to be a non-profit shell corporation. The same applies to MECG, whose counsel declined to name the client(s) it purports to represent during the questioning of Company witness Lobser. (Tr. 2370, l. 14 to 2371, l. 2)

IV. Rate Design/Class Cost of Service

a. Rate Design

i. Should a Revenue Stabilization Mechanism or other rate adjustment mechanism be implemented for the Residential and SGS classes for MGE and LAC? If so, how should it be designed and should an adjustment cap be applied to such a mechanism?

Argument: A statutory provision authorizing a revenue adjustment mechanism for residential and commercial customers like the one proposed by the Company in these cases has been in effect for over a decade. *See* Section 386.266.3. In the interests of moving towards more customer-friendly and easy to understand rate designs, as well as to further support efforts of customers to conserve energy, the Company is seeking a rate design that further aligns the

interests of the company and the customer – much to the disappointment of many of the intervenors to these cases who would seek to block such efforts for at least another decade. A significant majority of state utility commissions have adopted mechanisms that also adjust rates to address usage or revenue variations caused by weather conservation or customer levels. (Ex. 18, AGA Presentation). The Company's PGA/ACA clause has adjusted all sales customer rates for decades to ensure that fixed gas costs incurred by the Company are not over or under-recovered due to the impact of weather or conservation on revenues. And yet some parties to this case, including the Staff and OPC would have the Commission believe that it is simply not possible for the regulatory process here in Missouri to accommodate an adjustment mechanism that does the same exact thing for distribution revenues.

As stated in its opening statement on this issue during the evidentiary hearing, the Company has successfully collaborated with the Staff, OPC and other parties in the past to design rate solutions to the problems presented by weather and conservation and, if it must, it is prepared to continue its weather mitigation rate design, which all parties have agreed to in the past, and extend it to MGE. That solution, however, forfeits a unique opportunity to adopt a mechanism that would enable the Commission and the Company to respond to the desires that have been repeatedly expressed by customers and consumer advocates alike for lower customers charges and to more aggressively help customers conserve on the energy usage – all without exposing either the Company or its customers to the financial impacts of significant revenue variations from the levels authorized by the Commission in these cases. Some parties, like the National Housing Trust and the Division of Energy get it and have been helpful in seeking solutions.

The Staff and OPC, however, and even parties like MECG that would be unaffected by the RSM, continue to argue against it based on exaggerated claims about how the mechanism might capture immaterial revenue variations relating to customer switching and other factors. (Staff

Initial Brief, p. 54, OPC's Initial Brief, p. 33-34). The Company believes it has adequately addressed in its Initial Brief why these claims are both overblown and incorrect and do not provide a meaningful basis for determining that the Company's proposed RSM is not in full accordance with its enabling statute, Section 386.266.3. (See Company Initial Brief pages 76-79)[3] The Company will accordingly limit its reply to a few of the new matters raised by the Staff and other parties in their Initial Briefs.

First, the Company notes with disappointment that the Staff has rejected in its brief, every modification that the Company proposed to the Weather Normalization Adjustment Rider which the Staff submitted on the last day of the evidentiary hearing in this case. The Company is disappointed because this means that the Staff has proposed for the Commission's consideration a wholly inadequate alternative to the Company's proposed RSM that is really no alternative at all. While we're aware of no Missouri utility with a weather normalization mechanism, the Staff has professionals who are well versed in matters such as billing determinants and how a specific change to a specific rate component will affect the Company's revenues. Accordingly, the Staff must know that the proposal it offered, of a 1 cent per therm limit on any rate adjustment, would expose the Company and its customers to significantly more weather risk than they currently face today under the existing rate designs of LAC and MGE.

Moreover, while the Staff rejected the Company's $.05 cap, Section 386.266.3, like most weather adjustment clauses, imposed no cap at all. Staff seems to forget the nearly identical tools for rate

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[3]The Company would again refer the Commission to the Surrebuttal Testimony of Company Witness Scott Weitzel which demonstrates why such factors would have such an immaterial impact on usage. (Ex. 18, pp. 6-9). For example, even under the most implausible of circumstances where every new residential customer added by the Company had lower usage than the average residential customer, the effect on the average usage would be less than one third of a therm. (Id., p. 7, line 4-6). In reality, however, there will be new customers with higher than average usage to offset customers with lower than average usage and this already immaterial impact is likely to be even more marginal if not completely non-existent. Moreover, if customers switching between the SGS class and LGS class is really an issue, which the Company believes it is not, Company witness Lyons proposed customer charge modifications for these customers in his surrebuttal testimony that would make such switching even rarer. (Ex. 14, pp. 11-15)

adjustments available under the PGA/ACA mechanism for the Company and other gas utilities in Missouri. In fact, both LAC/MGE can file, in addition to the PGA and ACA, a Filing Adjustment Factor (FAF) or Unrecovered Actual Cost Adjustment (UACA) of up to $0.05 per therm or ccf when the Company is experiencing a significant over or under recovery of its gas costs. This tool is also symmetrical and credits can be issued to customers. As MGE's Tariff Sheet 15 states:

> PGA Filing Adjustment Factor (FAF) - In addition, in any PGA Filing, the Company may file a rate change (hereinafter referred to as the "PGA Filing Adjustment Factor" (FAF) not to exceed five cents ($0.05) per ccf which is designed to refund to, or recover from, customers any over- or under-recoveries of gas costs that have accumulated since the Company's last ACA Filing. The PGA Filing Adjustment Factor shall remain in effect until the next scheduled ACA Filing.

Similar language is also included in LAC's tariffs. (*See* LAC Tariff Sheet 28-C). The fact that these similar measures have been incorporated in MGE's and LAC's PGA/ACA tariffs for years, and have worked effectively for both the Company and its customers, demonstrates just how overblown the "chicken little" complaints by Staff are regarding the modest but necessary revisions that the Company has proposed be made to its Weather Normalization Rider.

The Staff is still excluding the SGS class from the RSM or the Company's modified WNAR even though 386.266.3 allows for "revenue effect of increases or decreases in residential and commercial customer usage due to variations in either weather, conservation, or both." Small shops and restaurants have similar weather and conservation trends as residential customers. In the Company's review of over 50 gas LDC's WNAR tariffs, only one company could be found that has an applicable class of residential only. The regulatory and industry standard is to have at least residential and SGS classes in WNAR. Again, another failure of the Staff to take a neutral and constructive approach to Missouri regulatory policy.

If Staff prefers that the Commission simply reject the RSM than it should just be forthright say just that; however, it was a strong supporter of a Straight Fixed-Variable rate design that accomplished the same thing, mitigating variances in base revenue from weather and

conservation, but not changes in customer levels – although through an unpopular 100% fixed charge rate design. The Staff should not, however, in the guise of providing an "alternative" to the RSM, recommend something on the last day of hearings that would sharply exacerbate rather than mitigate the revenue variation problem that Section 386.266.3 was designed to solve. That's too clever by half and a very unfortunate departure from previous efforts by the Staff, the Company and other parties to collaborate in seeking constructive solutions to this issue.

Other criticisms regarding the RSM proposed by the Company are equally baseless. For example, MECG argues that the RSM should be rejected because it is not "reasonably designed to provide the utility with a sufficient opportunity to earn a fair return on equity" as required by Section 386.266.4(1). (MECG Initial Brief, p. 46-47). According to MECG the Company has had sufficient earnings in the past and is likely over-earning now, so it doesn't meet this requirement. Of course, MECG provided absolutely no evidence to support its assertions regarding the Company's past earnings. Moreover, because the RSM would only adjust for variations from the level of revenue that was authorized by the Commission in a rate case where all relevant factors were considered, by definition, is reasonably designed to provide the Company with a sufficient opportunity to earn a fair return on equity (assuming other adjustments proposed in this case do not prevent such a result).

At the same time, multiple parties have suggested that if the Commission approves the RSM a downward adjustment should be made in the Company's ROE, presumably because it lowers the Company's risk of not achieving its ROE. (*See e.g.* Staff Initial Brief. P. 56; OPC Initial Brief. P. 35. Ex. 415, p. 8 l. 16-24; Consumer's Council Initial Brief, 3). In fact, the RSM will modestly help the Company achieve its authorized return when the weather is warm and help customers reduce their bills when the weather is cold and mitigate load loss for the energy efficiency programs it has already agreed to increase. Given these are symmetrical benefits for

both the Company and its customers, there is a sound justification for the RSM, but no justification for an ROE adjustment, All of the peer utilities used by the Company, Staff and OPC are either decoupled, have an RSM, or a Weather Normalization Adjustment Rider. Spire Missouri is the one outlier. It also already has in place significant mitigation for the 97% of usage variation noted by Staff from weather (Ex. 393, p.10), as well as mitigation for declining usage per customer, through a high customer charge and high initial block rate for LAC, and an even higher customer charge for MGE. All of its peer groups are either decoupled, have an RSM or WNAR.

For all of these reasons, the Commission should either approve the RSM proposed by the Company, with the constructive modifications that have been offered by other parties and accepted by the Company, or approve the Staff's proposed Weather Normalization Adjustment Rider with the changes suggested by the Company to make it a mechanism that will actually further the policy objectives of Section 386.266.3 rather than subvert them.

ii. Reflective of the answer to part i, what should the Residential customer charge be for LAC and MGE, and what should the transition rates be set at until October 1, 2018?

The Company believes it adequately addressed this issue in its Initial Brief.

iii. Reflective of the answer to part i, should LAC's weather mitigated Residential Rate Design be modified to collect a customer charge and variable charge for all units of gas sold, or should it be continued in its current form?

If the Commission does not adopt either the Company's proposed RSM or the modified version of Staff's proposed Weather Normalization Adjustment Rider, then it is imperative that the Commission not only permit Laclede to continue its Weather Mitigation Rate Design, which has been in effect for well over a decade, but also extend that same rate design to MGE.

V. Pensions, OPEBs and SERP

a. What is the appropriate amount of pension expense to include in base rates?

Executive Summary: Due to the Company's successful effort to control costs as discussed in the Introduction, there is, for the first time in many years, an opportunity to include in rates amounts sufficient to pay for current pension costs and to begin amortizing the pension regulatory asset that has accumulated over the past three decades, and to do so without a substantial rate increase. Although repaying past investments lowers rate base, and increasing current pension costs does not result in additional earnings for the Company, Spire Missouri believes the Company, employees and customers are best served by taking these actions at this time. The Company recommends including $31 million in LAC's rates, which is designed to fund 90% of pension liabilities, and $5.5 million in MGE's rates. These rates are designed to lower PBGC premiums and prevent another significant increase in these assets. USW 11-6 agrees with LAC and MGE. OPC also leans toward the Company's position. Staff agrees with the MGE funding level, but prefers to fund LAC's pension at the 80% ERISA Minimum level, which translates to $29 million.

Argument:

Nothing in Staff's brief changes the analysis of current pension expense recommended to the Commission in the Company's Initial Brief. Staff and the Company agree on MGE pension expense and are separated by $2 million on LAC's pension expense. LAC recommends $31 million, while Staff offers $29 million. (Staff Brief, p. 65) An important consideration in making this decision is the fact that over the past three decades, LAC has accumulated a large pension asset, which represents liabilities owed by customers for contributions LAC has made to its pension that have not been recovered in rates. OPC

recognizes that LAC's pension asset has grown to be quite large and opines that LAC's higher expense amount may be preferable because it would decrease the asset and save on PBGC insurance premiums. (OPC Brief, p. 37) OPC's reasoning is in concert with LAC's reasoning.

Staff states that LAC's solution to address pension issues "is to raise rates." (Staff Brief, p. 65) Staff appears to be critical of this position. It should be noted that Staff's successful effort to depress pension expense over many years has put us in the position we are today, with a $160 million pension asset. Staff's claim that the asset is only worth $131 million hardly changes this point.

Staff is also not persuaded by the fact that each $1,000 paid in pension expense would reduce PBGC premiums by $34. (Staff Brief, p. 66) Viewed a different way, each $1,000 paid by customers not only helps control the size of the pension asset, upon which LAC earns its weighted average cost of capital (WACC), but it is matched by the PBGC at the rate of 3.4%. Avoiding the additional cost of capital and obtaining a 3.4% match from the PBGC is a good reason for customers to invest the extra two million dollars.

The Company opposes OPC witness Pitts' suggestion for a strategic financing review of pension and benefit plans. (OPC Brief, pp. 35-37) The Company's pension and benefit plans already receive Board-level scrutiny and utilize some of the nation's leading investment advisory and actuarial firms to assist us in our stewardship of the plan assets while being mindful of each plans' liabilities and relative durations. Further, the Company has in the past, and will continue in the future to rationalize our employee retirement benefits as part of our overall employee compensation package. As we have grown, we have unified programs (to the extent permissible through collective bargaining) to gain economies of scale and minimize administrative fees. It should be noted that the MPSC investigated the pension plan practices of all the utilities in the state and didn't find any shortcomings on Laclede's behalf. (Ex. 20,

p. 11)

b. What is the appropriate amount of the LAC and MGE pension assets?

Executive Summary: MGE and Staff agree that MGE currently has a pension liability of (-$28.4) million. (Ex. 286, Acct. Sch. 02, p.1) LAC and Staff both agree that no appreciable asset accumulated under either FAS 87 or 88 between 1987 and 1990. Both agree to the amount of the FAS 87 asset between 1994 and 1996. Both agree to the pension asset that has accumulated since 1996 under both FAS 87 and 88. The amount of the pension asset agreed to is approximately $131.4 million. (Ex. 285, Acct. Sch. 02, p.1)

LAC maintains that between 1990 and 1994, it accumulated a pension asset under FAS 87 and 88 of $19.8 million. Staff disagrees. LAC maintains that between 1994 and 1996, it accumulated a pension asset of $9.0 million under FAS 88. Again, Staff disagrees. Together these two assets sum to $28.8 million, which is the amount of the dispute between the parties on this issue.

The question comes down to how much customers paid in rates for pension expense between 1990 and 1994, for both FAS 87 and 88, and from 1994 to 1996 for FAS 88. If rates had been set based on the Company's cash contributions to the pension plans, then customers had effectively paid the Company for its pension costs and no rate base asset should exist for those periods. But if customers had been paying the lower FAS 87/88 GAAP expense per LAC's books, then the customers owe LAC the difference between the lower GAAP expense and LAC's actual cash contributions. That difference is $28.8 million.

Boiling it down even further, the question is what did customers pay in rates in the 1990, 1992 and 1994 LAC rate cases? The answer is that LAC's true pension asset, based on what customers paid in rates for this period, is likely greater than the $28.8 million in dispute in this case.

Argument:

1990 Rate Case (GR-90-120)

Not only does the pension asset exist for the period 1990 to 1992, but if truly based on the likely amount provided in rates by customers, it would actually increase the size of the asset beyond the $28.8 million both parties believe to be at issue here. Staff states that a glance at the testimony supports its point that 1990 rates were based on cash contributions. (Staff Brief, p. 67) This interpretation falls apart when the facts are more closely examined. The Company stated in its Initial Brief that "there is no question that both LAC and Staff proposed rates to be set using FAS 87. Staff witness Rackers distinctly testified that Staff used FAS 87. (Ex. 45, p. 4, l. 13 to p. 5, l. 3)" While pensions are admittedly a complex issue, the question and answer by Mr. Rackers on page 6 of Staff's direct testimony in GR-90-120 is easily understood:

> Q. Has the Staff utilized the Statement of Financial Accounting Standards No. 87 (FAS 87) in its determination of pension expense?
> A. Yes, with regard to funded pensions.

(Ex. 276, p. 6, l. 22-26; and quoted in the Surrebuttal Testimony of LAC witness James Fallert, Ex. 45, p. 4, l. 14-23)

Since the pensions at issue here were funded pensions (i.e., not Board of Director Pensions or SERP), the answer then is simply 'yes.' (Id.) This should have immediately ended the debate with respect to 1990. But the Staff never even mentions this testimony, which is in its own exhibit (Exhibit 276), and in Mr. Fallert's surrebuttal testimony. Instead, Staff refers to Mr. Rackers' testimony on page 10 of Exhibit 276 to purportedly stand for the proposition that Staff used cash contributions to set rates. (Staff Brief, p. 67)

A closer review of the testimony in Exhibit 276 reveals Staff's error. FAS 87 is not a black and white number that can be pinpointed. Rather it is a methodology, which can produce different results based on the assumptions chosen. As stated above, on page 6 of his direct

testimony, Staff witness Rackers uses FAS 87 to set rates. On pages 7-9, he proceeds to explain the components of FAS 87 pension expense: Service Cost, Interest Cost, Expected Return on Assets, and Net Amortization. On page 9, Mr. Rackers then identifies the Company's three pension funds: Management, Contract, and Missouri Natural. Missouri Natural (MoNat) was a small gas utility LAC acquired in Southeast Missouri. It is less than 1/10 the size of LAC and has since been incorporated into LAC's tariff.

On pages 9-10, Staff witness Rackers proceeds to explain that he intends to choose assumptions under FAS 87 that will create adjustments to LAC's FAS 87 expense. In other words, Staff's FAS 87 expense will differ from LAC's FAS 87 expense, although both will be based on FAS 87. However, Staff decides that it is going to adjust the two larger pensions, Management and Contract, and not go to the trouble of adjusting the small MoNat plan. On page 10, Mr. Rackers explains that the Company's FAS 87 expense for MoNat is approximately equal to the cash contributions, so that neither an asset nor a liability was likely to be caused by reconciling cash contributions to FAS 87 expense. In other words, Mr. Rackers was effectively applying the 80-20 rule by adjusting FAS 87 for the two big pensions, and not bothering with the small pension. (Ex. 276, p. 9, l. 23 to p. 10, l. 8.) This is the section that Staff cites for the proposition that rates were set on cash contributions. Nothing could be further from the truth.

Proceeding to page 11 of Mr. Rackers' testimony, he decides to adjust the FAS 87 component Expected Return on Assets by using the "actual fair market value" rather than the Company's "market-related value." Mr. Rackers implies that the Company was trying to use market-related value to obtain a higher pension expense in rates. He noted that his adjustment "results in…a reduction in pension expense." (Id., p. 11, l. 8-15) In other words, Staff was lowering the Company's cost of service by lowering its pension expense, based on FAS 87 and not cash contributions.

Page 12 shows that using fair market value results in a $21 million increase in asset value which, at an 8.25% return rate, results in a pension expense reduction of about $1.7 million. (Id., p. 12, l. 2-27) Mr. Rackers notes that he could have used a 16% return rate, which would have multiplied the adjustment ten-fold, but he decided to be conservative in the reduction "due to the modest revenue requirement increase which Staff is currently recommending…and the financial impact [i.e.,$18 million] which this additional adjustment would have…" (Id., p. 13, l. 22 to p. 14, l.2; p. 15, l. 1-7)

Staff proceeded to make another FAS 87 adjustment on the "corridor" amount which, along with the impact of the above-mentioned use of actual fair market value on amortization, reduced pension expense by the sum of $2.5 million. Other changes further increased the pension expense reduction, such as shortening the amortization period. Suffice it to say that the Staff's FAS 87 adjustments sponsored by Mr. Rackers significantly reduced FAS 87 expense. (Id., pp. 16-18)

Both Staff and the Company filed testimony setting pension expense based on FAS 87. However, due to Staff's adjustments, Staff's FAS 87 expense level was significantly lower than LAC's FAS 87 expense level. Since the case was settled, it is impossible to know exactly what amount of FAS 87 expense went into rates, although it is reasonable to assume that it was less than LAC's number and possibly higher than Staff's number. However, since LAC bases the pension asset on the difference between LAC's cash contributions and LAC's FAS 87 expense, the actual expense in rates should have created a larger asset because rates would have reflected a lower FAS 87 expense than on LAC's books.

In summary, pension expense in the 1990 rate case was unquestionably based on a FAS 87 calculation, as clearly testified to by Staff witness Rackers, and not a cash contribution basis as Staff tries to argue in its brief. Not only did the asset accrue based on the difference between

cash contributions and FAS 87 expense, but given the Staff's adjustment to FAS 87 expense, the true amount of the asset, based on what customers actually paid in rates, was probably larger than the amount that resulted in the $19.8 million for the period 1990-1994.

1992 Rate Case (GR-92-165)

Having erred with regard to the facts of the 1990 case, Staff's version of the 1992 case is much more accurate. Both Staff and LAC filed their cases based on cash contributions, and the parties to this case agree that they did so because in a 1991 KCPL rate case (GR-91-291), the Commission approved rates based on cash contributions. (Staff Brief, p. 68). However, as stated in the Company's brief, both Staff and LAC agreed in the 1992 case that they needed an express Commission order under FAS 71 to be able to move from FAS 87 GAAP accounting to cash contribution. LAC formally requested such an order in the direct testimony of LAC witness Mark Waltermire (Ex. 45, p. 5, l. 8-21; Ex. 278, p. 3, l. 1-6, p. 9, l. 9 to p. 10, l. 2). However, the case settled without the Commission approving an order allowing LAC to implement FAS 71. In the absence of such an order, pension expense continued to be based on FAS 87 and FAS 88. To believe that rates were based on cash contributions requires the Commission to believe that LAC and Staff made such a change without obtaining the order both acknowledged was needed. As evidence of what such an order would look like, once Staff agreed to base rates on cash contribution in LAC's 2002 rate case, the Commission's order was very explicit in approving it. (Ex. 45, p. 3, l. 20 to p. 4, l. 2; GR-2002-356, Order Approving Stipulation and Agreement, dated October 3, 2002, p. 5, and Partial Stipulation and Agreement dated August 20, 2002, p. 4) Again, LAC's pension asset would at least have been conservatively based on LAC's generally higher calculation of FAS 87 and FAS 88.

1994 Rate Case (GR-94-220)

In this case, LAC filed pension expense based on FAS 87/88. Staff witness Young claimed that neither party itemized a pension asset in rate base during these cases. As demonstrated at hearing, LAC included its full pension asset in its schedules in the 1994 rate case. (Ex. 62) Staff's response was that "Spire's exhibit is not irrefutable evidence that rates included a deferred asset in the 1994 case. Instead, Spire's exhibit serves to illuminate the reason Staff chose to explain its support for a pension asset in rate base in LAC's subsequent rate case in 1996." (Staff Brief, p. 69)

LAC agrees that Exhibit 62 is not irrefutable evidence that 1994 rates included the disputed deferred asset. That the rates have not included the deferred asset is precisely the problem. Exhibit 62 is irrefutable evidence that Staff's testimony is wrong in claiming that LAC did not itemize its pension asset in its 1994 rate case filing. It is irrefutable evidence that LAC tracked the pension asset, and tried to recover it in rates in the 1994 case. As stated in Staff's brief, there has been a longstanding practice of LAC including the asset in rate cases and Staff removing it. (Staff Brief, p. 70). The matter has never been put in front of the Commission for decision, until now.

LAC and Staff agree that 1994 rates were set based on FAS 87 expense, and they agree to the amount of the FAS 87 pension asset that has accrued since 1994. However, Staff is also arguing that FAS 88 gains were not flowed to customers through lower rates in the 1994 rate case, so the Company should not have accrued a $9.0 million FAS 88 asset over the 1994-96 time frame.

Staff makes virtually no argument against this asset, because it has no argument. In response to LAC witness James Fallert asserting LAC's right to the FAS 88 asset in rebuttal testimony (Ex. 44, pp. 6-7), Staff does not even mention the $9.0 million 1994-96 FAS 88 asset in summarizing its position in surrebuttal. (Ex. 263, p. 7, l. 15 to p. 8, l. 5) Nor does Staff

mention the $9.0 million 1994-96 FAS 88 asset in the four pages of its initial brief dedicated to this issue. (Staff Brief, pp. 66-70).

In contrast, Spire Missouri's initial brief lays out several reasons why the FAS 88 gains were used to lower rates in 1994, reasons that justify LAC recovering the resulting pension asset for the period 1994-96 in rates. These reasons included: (i) the unavoidable fact that in Case No. GR-94-220, Staff witness Boczkiewicz discussed how he normalized FAS 88 gains in Staff's rates (Ex. 45, p.6, l. 11 – p. 7, l. 11); (ii) the fact that, due to the close link between FAS 87 and FAS 88, the Company would not use FAS 87 in rates without also applying FAS 88 (Ex. 44, p. 6, l. 15 - p. 7, l. 2); (iii) the Report and Order in LAC's 1996 rate case (GR-96-193) stated that the Commission was granting LAC authorization to *continue* to utilize FAS 87, 88 and 106 for regulatory purposes, indicating that FAS 88 was already being used to set customer rates (Id., p.7, l. 3-9); and (iv) in the 1994 case, Staff initially filed its case on a cash contribution basis, but when a change in law occurred (HB 1405), Staff changed its position to use FAS 87 and FAS 88 for ratemaking. (Ex. 45, p. 6, l. 4-10) These reasons provide indisputable proof that FAS 88 gains were used for ratemaking in the 1994 case, and that LAC should be able to recover the $9.0 million asset that accrued as a result of customers' enjoyment of those gains.

In summary, it is clear that FAS 87/88 expense was used in the 1990 and 1994 rate cases. It is also clear that FAS 88 gains were included in 1994 rates. FAS 87/88 was also used to set rates in the 1992 rate case, unless the Commission is willing to believe that Staff and the Company applied non-GAAP rates without the Commission's approval.

Because LAC is applying for its first non-ISRS rate increase in 7½ years, and has created significant cost reductions for customers, LAC seeks to have this issue finally resolved in this case. If favorable, LAC could begin the process of amortizing this long-held asset in rates. If

unfavorable, LAC could be faced with a $28.8 million write-off. (Ex. 44, p. 8, l. 3-7) Under the circumstances, LAC is amenable to a normal pension asset recovery period, or a recovery period as long as 20 years. The return the Commission may grant on this asset is not as important to the Company as obtaining a return of the disputed amount and resolving this longstanding issue.

Finally, the Company opposes OPC witness Pitts' recommendation of a $54 million reduction in the pension asset to reflect amounts allegedly contributed in excess of the ERISA minimum. (OPC Brief, pp. 38-39) The Company addressed Mr. Pitts' error on this point in its initial brief, noting that in every proceeding since we have been on a "funded" basis, the Staff has reviewed actuarial reports and received copies of all contributions made into the trusts. Each contribution has been property vetted. Finally, and most importantly, the reality is that past contributions made have resulted in the current funded status and funding requirements. Had such contributions not been made in the past, the current funding requirement needed would have been just that much higher. (Spire Missouri Brief, pp. 94-95)

c. How should pension regulatory assets be amortized?

Executive Summary and Argument: The Company appreciates OPC's flexibility on this issue. All three parties are now in agreement that an amortization of eight years is acceptable. Both the Company and OPC are willing to support a 10-year amortization if that is the Commission's preference. Either way, the Company's success in controlling costs over the past several years will avoid any rate shock for customers regardless of the length of the period the Commission chooses to amortize this substantial asset. The Company again notes that increased pension rates are accompanied by an increased expense, so these funds are a source of cash but do not increase the Company's earnings.

d. What is the appropriate amount of SERP expense to include in base rates?

Executive Summary and Argument: The Company and Staff both agree to the amount of $468,731 for SERP. OPC argues that the amount should be $24,000. (OPC Brief, p. 40) In its brief, Staff skillfully anticipated and answered all of the positions taken by OPC witness Hyneman and included in OPC's brief. (Staff Brief, pp. 71-75) For the reasons discussed in the initial briefs of Spire Missouri and Staff, the Commission should include $468,731 in rates for SERP expense.

e. Should SERP payments be capitalized to plant accounts?

Executive Summary and Argument: All three parties agree that SERP payments should not be capitalized. And in fact the Company is not capitalizing payments made under its SERP program. (Ex. 21, p. 18) Therefore, the Commission should deny OPC's recommended adjustment of $461,279.

The Company's books reflect SERP costs on a FAS 87 basis according to GAAP. Such costs are booked on an accrual basis over the service life of the employee. We capitalize this FAS 87 accrual in accordance with the USOA, as required. Staff agrees that GAAP allows for the service cost component of FAS 87 SERP expense to be capitalized. (Staff Brief, p. 75)

f. Should the prepaid pension asset be funded through the weighted cost of capital or long-term debt?

Executive Summary: Staff and the Company both agree that the pension asset should earn the normal weighted average cost of capital (WACC). OPC takes the extreme position of ignoring precedent and demanding these assets get less recovery due to what they feel is the low-risk nature of these rate base investments. OPC's position regarding low-risk is counter-intuitive given their efforts to disallow and write-off over $80 million of this asset. (Spire Missouri Brief, pp. 93-95; Staff Brief, p. 71) Because cash is fungible, the amount advanced by investors to fund the pension is just like amounts advanced by investors to fund

other capital purchases, such as vehicles. The pension asset should not be singled out for a return based only on debt, just like it should not be rewarded with a return based only on equity. Like all assets in rate base, the pension asset should earn a return based on the Company's WACC. Investors do not pick and choose what assets they invest in. They simply invest capital in the Company and expect to receive the Company's overall cost of capital in return.

Argument:

In its brief, OPC could only cite one state, Colorado, where the Commission has approved the fiction that the pension asset should earn a lower return than other assets. (OPC Brief, p. 42) In the Colorado decision cited by OPC, the Commission gave no explanation for its unusual action other than it found merit with the Staff and OCC's recommendation. (Id.) Although OPC stated that "some regulators do not believe the prepaid pension should receive rate base treatment," the citation to OPC witness Pitts testimony named no such regulators. (Id., p, 43)

OPC's claim that pre-paid pension assets are not used or useful in the delivery of utility service is basically an argument that the people employed at Spire Missouri to whom those pension obligations are due do not contribute to the delivery of utility service. (Id.) This is both an insulting and senseless argument. OPC witness Pitts makes even less sense in arguing that the return on pension assets should be reduced because the PBGC insures qualified pension benefits in the event that the plan sponsor cannot meet its obligations. (Id.) Mr. Pitts misses the fact that the plan sponsor being unable to pay is not the issue. Rather the issue is that the plan sponsor's investors have already advanced the money to the pension, and the plan sponsor needs to collect the funds to repay them. Mr. Pitts' argument essentially is that customers do not have to pay the overall cost of capital to the Company for these rate base

investments, because if the Company fails, an insurance company will pay the Company's employees.

Most astonishingly, OPC takes contradictory positions in this effort to prevent the Company from recovering its investments and cost of capital by referencing an isolated precedent from another state. "Comparably, in Missouri, ratepayers would be essentially guaranteeing the company **timely** and **whole** recovery of costs through the current rate base recovery mechanism. Therefore, the lower associated risks should support a lower return." (page 42, emphasis added) Again, to understand the extreme and contradictory positions, view this statement in conjunction with OPC's proposal to draw out recovery of these assets over two decades (certainly not timely) and to disallow and write off over $80 million, or roughly half of these investments (certainly not whole).

As Spire Missouri stated in its initial brief, Mr. Pitts' recommendation is nothing more than an opportunistic and very transparent way of lowering the asset return in a way that is inconsistent with the Stipulation and Agreements signed by the Company, Staff and OPC over many years. Those stipulations specified that the asset would receive rate base treatment, with the understanding that such treatment would be at the weighted average cost of capital. (Ex. 20, p. 12, Sch. GWB-R2) The witness' claim that pension funding is risk free is belied by the fact that he is putting millions at risk with his reduced return plan.

VI. Income Taxes

b. What is the appropriate amount of accumulated deferred income tax to include for LAC and MGE?

As indicated in its Initial Brief, the Staff and Company have agreed that a combined $344 million in accumulated deferred income taxes ("ADIT") should be reflected in the cost of services of LAC and MGE. In its Initial Brief, however, OPC has proposed the

Commission recognize for cost of service purposes, not only the $344 million in deferred taxes that the Staff and Company have agreed is appropriate, but also an additional $54 million in ADIT relating to open years that "open" years – i.e. years in which an adjustment could still be made by the IRS to reverse an "uncertain" tax position that the Company has taken to generate these amounts. (OPC Initial Brief, pp. 43-46)

This reckless and unnecessary recommendation should be rejected by the Commission. OPC's speculation at page 46 of its Brief that Commission can reflect such ADIT amounts now because the Company could someday seek to recover its losses if the IRS were to then reverse these deductions (after all appeals were exhausted, of course) is not anywhere close to being a sufficient or reliable enough remedy to induce the Company into taking similar actions in the future. Nor does it protect customers from the loss of the Company's ability to use these kind of tax approaches in the future to benefit them in the substantial way they have in these cases. Similar to other positions, OPC seeks to take the benefit and ignore the cost. If the Company were to reflect these positions without also recognizing the Net Operating Losses (NOLs) of $63 million, it would create a normalization violation, which would cause the Company to not be able to take advantage of other beneficial tax positions, like accelerated depreciation, which represents much of the remaining ADIT balance. Also, these tax positions essentially caused the NOLs and to include one without the other would clearly create a normalization violation. Also, because the Company has reflected these NOLs, it has not received cash related to these positions. The benefit of the tax position is suspended with the NOL and until the NOL is utilized the benefit will not be realized. The Company treated both of these items as not part of the rate base offset.

It should be noted that the Company's customers will ultimately receive the full benefit of these tax positions once the years in which they were generated are closed (meaning no

longer subject to a possible reversal by taxing authorities) and the Company's rates are subsequently changed. In the meantime, however, customers are already benefiting from nearly $100 million in rate base offsets for the closed years, and attempting to recognize the open year tax deductions now would expose the Company to a significant monetary loss and its ability to use these kind of tax positions to benefit customers in the future.

It is for this very reason, as OPC notes, that the Commission rejected premature recognition of these kind of uncertain income tax deductions in its January 27, 2009 Report and Order in ***Re: Union Electric Company, d/b/a AmerenUE***, 18 Mo.P.S.C.3d 306, 348, Case No. ER-2008-0318. As stated in that Report and Order, the Commission took this prudent course and did not unnecessarily expose AmerenUE (and potentially its customers) to significant financial jeopardy because "Both ratepayers and shareholders benefit when AmerenUE takes an uncertain tax position with the IRS, saving money on taxes benefits the company's bottom line and reduces the amount of expense the ratepayers must pay." (*Id*. at 348).

The Commission should approach this issue in the same way as it did in the AmerenUE case and reject OPC's overreach. Ratepayers are already receiving a substantial benefit in these cases of some $344 million in rate base offsets due to the Company's assertive use of existing tax laws. This does not even include the flow-through benefits customers have benefited from on current taxes because the Company has integrated MGE operational practices in a way similar to LAC, which lowered their effective tax rate to less than 32%. For all of the reasons, OPC's proposal to include these additional amounts in Company's cost of service should be rejected.

VII. Incentive Compensation for Employees

a. **What is the appropriate amount of employee incentive compensation to include in base rates?**

b. **What criteria should be applied to determine appropriate levels of employee incentive compensation?**

Spire Missouri will address these sub-issues together since the Company's response to part a corresponds to Staff's brief in part b.

Executive Summary: The appropriate amount to include in base rates would be the amount in Staff's EMS runs, plus the $6.84 million disallowed by Staff ($8.855 million, less a $2.018 million adjustment to put back in Union incentives). Offering employees the opportunity to earn a portion of their compensation through market-based incentives is a common, prudent and wise way to operate a business and attract, retain and motivate qualified applicants and has created tangible, significant benefits for customers. Such a balanced incentive program better aligns the interests of employees with the customer and the business. As a result of employees' efforts, the Company has made its operations more efficient, lowering its historical inclining cost profile as evidenced by the modest rate increases requested in these cases after four years, and improved its service - all successes achieved through the efforts of employees who are paid market-based compensation through a package of base salary and incentives. It is only reasonable for customers who benefit from these improvements to pay the market value compensation of the employees who produced them. This should include all the hard-working employees of the Company, from the entry level clerks to the executives.

Argument:

Spire Missouri opposes the position of OPC, and agrees with the position of Staff to approve all incentive compensation, both earnings-based and performance-based, for the Union. (Staff Brief, p. 78; OPC Brief, p. 51) Staff's position is consistent with the statute that

prohibits rates that change employment conditions subject to collective bargaining. (Section 386.315 RSMo.) Staff believes its position will eliminate the Union's concerns. This appears not to be the case, however, because as discussed in the Introduction above regarding the cooperative spirit at Spire, the Union's Brief evoked a concern that the Company recover the costs of its management incentive program as well as the Union's incentive program. (Union Brief, pp. 3-4)

The Staff's brief proceeds to address the performance-based component of the management Annual Incentive Program (AIP), and cites its witness, Mr. Young, to support its criticisms of the Company's plan. (Staff Brief, pp. 78-87) Spire Missouri addressed the bulk of these issues in detail in its initial brief (Spire Missouri Brief, pp. 96-101)

Staff stated that the Company's AIP "does not meet prior Commission standards, and should be excluded from rates." (Staff Brief, p. 78) However, the most recent Commission pronouncement on standards for performance-based and earning-based incentive compensation are found in the 2009 Ameren Order. (Ex. 70) Staff did not mention this case in its direct testimony or in its surrebuttal testimony on this issue. And in the nine-page discussion of performance-based incentives in its brief, Staff does not even mention the 2009 Ameren Order until the final paragraph. (Staff Brief, p. 86) In that paragraph, Staff picks out one point from the 2009 Ameren Order, the conclusion that the overall program must be acceptable to be included in rates. (Id.) Staff entirely misses or ignores the detailed guidance provided by the order in how Staff should approach the performance-based portion of a utility incentive compensation program. Spire Missouri discussed this in its brief. (Spire Missouri Brief, p. 100)

In the 2009 Ameren Order, the Commission noted that Staff's witness in that case, a Utility Regulatory Auditor with no real expertise in compensation plans, was not qualified to

critique a utility's plan in detail. The Commission found it to be akin to the Staff designing a compensation plan, and noted that Staff should not be trying to do that. Rather, the Commission advised, Staff must evaluate these programs at a higher level and not get bogged down in the details. (Ex. 70, pp. 89-90) In this case, Staff witness Young, also a Utility Regulatory Auditor, attempted to do exactly what the Commission counseled against - evaluate the Company's incentive compensation program at a detailed level.

Worse, Mr. Young attempted his evaluation based on information that only scratched the surface of the program. He had asked for and received 6,500 objectives for Company employees, but he didn't choose to follow up to seek explanatory details on a sampling of those objectives or, most importantly, the performance metrics that would have revealed the specific and measurable levels of achievement and the difficulty of meeting the three performance levels. The fact that the witness didn't know what he didn't have proves the Commission's point in the 2009 Ameren Order – that Staff should not be trying to critique the quality of a plan.

Naturally, Staff tried to blame its lack of information on the Company's failure to produce it. (Staff Brief, p. 82) However, the Company had no reason to withhold this information. Mr. Young asked for objectives, and the Company produced 6,500 of them, organized by employee number, department and weighting. (Tr. 2704-06) If Mr. Young wanted to review more information he could have asked for it. Having audited KCPL's incentive compensation plan twice, he should have known that there was more to Spire Missouri's plan then a list of objectives.

Certainly, the Company anticipated that Staff would want to know generally how the incentive compensation program worked – Were there objectives? How are the objectives determined? Are the objectives weighted? How are the performance levels set? What is the

process for evaluating the employee's performance? Mr. Young asked many of these process questions in data requests, and knew the answers in his testimony and when asked in cross-examination. (Ex. 205, p. 103, l. 1-7; Tr. 2707, l. 12 to 2708, l. 6) Under the 2009 Ameren Order, the auditor's efforts in confirming the process should have sufficed. Regardless, it is not up to the Company to answer data requests that haven't been asked, or to anticipate that a Utility Regulatory Auditor would want to do an in-depth, point-by-point analysis of an incentive compensation program designed and implemented by people like Company witness Mispagel, who has extensive experience and expertise in the compensation and benefits field. And it is not up to the Company to anticipate that an auditor would do so despite the Commission admonition in the 2009 Ameren Order to avoid getting bogged down in details. (See Staff Brief, p. 83)

The roadmap Staff witness Young chose to use was from a 1987 Commission order, which he cited as requiring improvement over existing performance. (Staff Brief, p. 79) As explained in Spire's brief, and agreed to by Staff at hearing, one cannot be expected to ever improve existing performance. (Spire Missouri Brief, pp. 99-100) However, Spire Missouri's AIP requires employees to perform beyond normal expectations to qualify for incentive compensation above the 100% level.

The Staff witness made other mistakes that are simply a function of the fact that he is not an expert in the compensation and benefits field. For example, he claimed that once an employee reaches a level where no improvement is possible, individual metrics should begin focusing on another area of concern. (Staff brief, p. 80) If one of a team's goals is to minimize accidents, just because they may have had a year with zero accidents doesn't mean they should stop pursuing that goal.

If Staff, as a neutral party with no substantive interest, really wanted to explore Spire

Missouri's incentive compensation program, Spire provided a compensation and benefits expert with 30 years' experience in the field to testify at hearing. Staff's questioning of this expert consisted of 13 lines on page 2679 of the transcript. In that short colloquy, Staff's main goal appeared to be to establish that Staff had unilaterally reversed the Commission's 2009 Ameren Order by stopping Ameren from collecting earnings-based compensation in rates through a stipulation in a later case. Since a financial metric is a necessary component of a balanced program that targets both improved service and decreased cost, it can only be concluded that it is the actions of Staff in eliminating such metrics that are detrimental to customers, and not the actions of Spire Missouri, or Ameren.

On pages 84-85 of its brief, Staff asserts that Spire Missouri should not recover costs for performance that applies to non-regulated activities, or non-Missouri regulated activities. Spire Missouri agrees, and the amount requested by the Company in rates include only the portion of incentive compensation allocable to Missouri utilities. In its brief, Staff mentions an employee objective that clearly comes from an employee involved in lobbying activities. (Staff Brief, p. 86) Staff knows full well that half of this employee's compensation, including incentives, is removed from rates to acknowledge that lobbying activities may not benefit customers. In effect, Staff is advising the Commission to exclude a program based on an objective that it knows is not in rates. Staff's witness agreed at hearing that the Commission should not judge the program based on objectives weighted at 0%. (Tr. 2702-03)

The final standard that Staff addresses in its brief requires the incentive compensation package be linked to overall customer benefit. They state that "an acceptable management performance plan should contain goals that improve existing performance" and have concerns that "individual goals can be structured in a way that leads to deterioration of service quality, like substantially cutting costs in the customer service area that could result in a reduction to

customer service quality." (Staff Brief, pp. 85-86) This is echoed by OPC who states "this Commission has held over many years that earnings and equity-based incentive compensation provides not only zero ratepayer benefit but results in a ratepayer detriment and therefore should not be included in utility rates." (OPC Brief p. 50) Despite steadfastly assessing other costs based on a "known and measurable" standard, both groups seem to completely ignore the significant customer benefits related to customer service, business process and systems improvements, along with tens of millions of dollars in annual cost savings that have actually been achieved by the employees of the Company. These savings and improvements are both known and measurable. But instead of approving the market-based compensation costs that drove these savings, Staff and OPC seek to disallow them – all because a different mix of incentives **could** result in a customer detriment sometime in the future.

At what point will either group acknowledge that the way to obtain cost control for customers without sacrificing service quality is to have a balanced scorecard that incentivizes financial goals as well as performance? Spire Missouri understands this, and has come into this case demonstrating improved performance metrics and unprecedented cost containment. The Commission understands this, as reflected in its 2009 Ameren order. The Staff refuses to remove its blinders, and has even overruled the 2009 Commission. At what point will they stop ignoring the facts about the benefits of financial metrics in a balanced program, and start supporting programs that unquestionably benefit customers? The Commission should require Staff to explain how eliminating financial goals from a balanced program benefits customers.

Finally, in the last paragraph of this section, Staff addresses the 2009 Ameren order. (Staff Brief, p. 86) Staff declares that Spire Missouri's incentive compensation fails overall because it is 50% based on earnings and 50% based on faulty performance metrics. (Id.) In the Company's view, the balance between financial and performance metrics is a strong

advantage for the program, and is, and has been, a benefit for customers.

c. **Earnings Based Incentive Compensation – Should LAC and MGE be permitted to include earnings based and/or equity based employee incentive compensation amounts in base rates?**

Executive Summary: The Commission should include in rates the expenses related to incentives, whether equity or earnings-based, so long as the overall compensation package is market-based to attract, retain and motivate employees, and is balanced in its approach to create meaningful benefits for customers. Spire Missouri's regulated revenues are based on its cost of service. If employees can increase the Company's earnings by controlling those costs, customers will benefit. In fact, customers are already benefitting from incentives through less frequent rate cases, and are benefitting in these rate cases through rates that are lower than they would otherwise be. Likewise, employee efforts that increase revenues by activities such as customer growth, also benefit customers, because more revenues for the Company means less the customer will pay in increased rates. The Commission has previously approved incentive programs with an earnings component when accompanied by service and operational components in a 'balanced scorecard.' (See Ex. 70, *re: Ameren*, Case No. ER-2008-0318, Report and Order dated January 27, 2009)

Argument:

1. Management Earnings-based Portion of AIP

Spire Missouri has addressed much of Staff's Brief in its initial brief. Staff recites the regulatory history of earnings-based incentive compensation, but again does not come to the key 2009 Ameren Order until page 91, halfway through the eight-page section. Staff includes a quote from a 2004 MGE rate case stating that the shareholders that benefit from a financial incentive compensation plan should pay the cost of that plan. (Staff Brief, page 88) There is

appeal to an approach in which the beneficiary pays the cost. It has been established in this case that since an incentive plan places pay at risk, the base pay with no incentive is less than the employee's normally expected compensation. So, there is no question that charging in rates only the base salary is clearly undercompensating the Company. It has also been established in this case that payment at 100% of target is equivalent to a normalized level of market-based total compensation. Payment at this level would be a fair charge to the customer and would fairly compensate the Company. Finally, it must be conceded that payment of more than 100% of target indicated an above expected result for the Company, which benefits the shareholder very briefly if it occurs in the test year, and for a longer period if it is outside of a test year. So the simple answer to this conundrum appears to be that the customer should pay at the 100% target level, which is the market-based level for total compensation and the employee's normal expected compensation.

In the end, the customer should come out ahead because people react to incentives, meaning they will make the effort to come out at or above 100% more often than not. The Company will bear the extra compensation costs and keep the extra earnings until the next rate case, when the customer will reap the benefit of reduced costs.

In other words, the customer would pay to the 100% target level but no more. This would be fair to both sides and would at last free us from the continued burdens of making and responding to arguments that strain common sense and logic, such as "customers don't benefit when costs are reduced relative to revenues." In addition, it would allow us to continue our balanced incentive programs that have clearly proven in this case to be beneficial to customers.

The 2009 Commission allowed Ameren to recover the cost of its management incentive program because the overall program was not funded purely by financial incentives, but by a mix of earnings and performance metrics. The implication is that anything under 100%

financial should not be automatically dismissed. (Ex. 70, pp. 90-91) In fact, a 50-50 plan should be considered *more* balanced, and therefore preferable to a plan that is only 25% earnings based. (See Staff Brief, p. 92)

On page 93 of its Brief, Staff slips back into arguments on performance metrics that are either illogical or mis-stated. For example, Staff states that "Spire Missouri has argued it does not agree a goal must require improvement." (Staff Brief, p. 93) It has already been discussed above that attainment of more than a 100% payout should require superior performance, regardless of whether the performance exceeds that of the previous year. Staff is also critical that an employee who hasn't quite met target expectation could earn an incentive of between 50-100%. However, that level would result in the employee earning less than the expected market compensation for a job that did not meet full expectation. Staff's argument lacks an understanding of compensation concepts. Finally, Staff improperly compares the maximum level for Ameren's program to the target level for Spire Missouri. Ameren's maximum is "very difficult to achieve." (Id.) So is Spire Missouri's maximum of "Outstanding Performance". Staff though is critical of Spire Missouri witness Mispagel's statement that Spire Missouri's goals are attainable. Staff mis-states the quote and misunderstands the difference between maximum (150% in Spire's program) and target (100%). Mr. Mispagel actually testified that "Target levels…are challenging, yet attainable, and the target level may not be achieved all of the time." (Ex. 48, p. 6) Attainability is actually one of the core concepts of the incentive program, because a non-attainable goal is demotivating.

Staff makes another serious error in comparing Spire Missouri's incentives to the 2009 Ameren Order. Staff accurately quotes the order as prohibiting purely financial incentives. Based on that direction, Staff disallows Spire Missouri's earnings-based compensation. (Staff Brief, p. 94) In other words, Staff disqualifies a 50% financial – 50% performance based AIP

program, because the 50% financial portion is 100% financial. This attempt at designating a 50% financial program as ”purely financial” defies logic and fails to assess the whole program.

Finally, Staff proudly boasts that in the wake of the Commission’s 2009 Ameren Order, it has overruled the Commission by somehow getting Ameren to accept Staff’s adjustments eliminating the 25% earnings-based metric, “the very ones discussed in the 2009 Report and Order.” (Staff Brief, p. 94) According to the Commission’s website, Staff is supposed to be a neutral party without a substantive interest, tasked with the duty to provide expert policy advice to the Commission. Instead, Staff is not only an advocate on certain issues, but is not afraid to reverse Commission policy when it believes the Commission has erred.

In the end, Spire Missouri agrees that customers should pay a target compensation level for targeted results of a balanced overall program, even if that program includes earnings metrics, but should not pay for above target compensation, even though any associated service performance benefits customer and even though savings ultimately lowers revenue requirement.

2. Earnings-based equity compensation

Staff is correct that the 2009 Ameren Order would not permit recovery of the Company’s Equity Incentive Program (“EIP”), because it is 100% based on earnings related metrics. However, as Spire Missouri noted in its brief, the EIP is awarded in stock rather than cash, and has a longer-term view. Its incentives encourage retention of key upper management employees, improved earnings and relative shareholder value. (Ex. 205, p. 105) As demonstrated above, all three of these components benefit customers as well as shareholders, and as noted, Spire’s track record has shown considerable benefit for customers that are known and measurable.

Executive incentive pay has been the most controversial for the commission to

approve. (Ex. 70, pp. 85-86) However, in this particular case, the incentive provided to Spire executives may have been the most important one for customers. For example, over the past several years, executives at Laclede, including the CEO, have received incentive compensation for meeting growth objectives. Growth arose from Laclede's acquisitions of MGE, Alagasco, Mobile Gas and Willmut Gas. Instead of the approximate 630,000 customers Laclede had prior to September 2013, the Company now serves 1.7 million customers in three states. This growth has allowed the Company to increase its earnings by spreading its costs across a broader customer base, thus lowering its cost per customer. These higher earnings result in lower costs for customers, a benefit customers have enjoyed in the form of lower rate increases sought less frequently. Growth has also created scale to develop and invest in more modern, capable and efficient managerial and technology platforms for the business, which has allowed the Company to leverage operational efficiencies and knowledge across its expanded footprint, also benefitting customers. It is not unfair for Spire Missouri to ask customers to pay for the compensation that motivated the achievement of those customer benefits. (Ex. 48, pp. 8-9)

d. **Should LAC and MGE be permitted to capitalize earnings based and equity-based employee incentive compensation amounts in base rates?**

Executive Summary: Employee compensation is charged to a mix of capital and expense, in accordance with GAAP and based on the employee's function. All permitted compensation should follow the same capital-expense path, including base wages and salaries, performance based compensation and earnings based compensation. The Commission should not make an adjustment to any of these capitalized amounts, and should certainly not adjust amounts capitalized prior to the effective date of rates resulting from the stipulations and agreements in the previous rate case.

Argument:

Spire Missouri covered the arguments of Staff and OPC in its initial brief. However, Staff added an argument that the Commission should remove incentive compensation from capital because Staff forced Ameren to do so in the same 2011 case discussed above in which Staff reversed the Commission's policy of allowing a mix of earnings-based and performance-based incentive compensation in rates. (Staff Brief, p. 95) The Commission should not countenance Staff's brazen act, and should instead approve Spire Missouri's capitalized incentive compensation, along with its balanced AIP that has brought service and operational improvements to customers at a cost that is lower than it otherwise would have been. There is simply no reason to interfere with a business model that is working so well for customers, and no reason that customers should not pay for the costs to keep the model going to create further win-win results.

e. To the extent the Commission declines to include employee incentive compensation in rates, what adjustment should be made to base salaries paid to employees?

Executive Summary: In the absence of an earnings based incentive program in the market, the Company would have to substantially increase its base pay in order to attract employees. Such an increased base salary at a market rate would almost certainly go unchallenged by Staff. However, Spire Missouri prefers to manage through incentives that are designed to also align the interests of employees and customers and enhance performance levels. The Company would agree to incentive compensation in rates equivalent to the 100% target rate, which is, by definition, what current employees would receive if they performed at expected levels.

Argument:

While the Company disagrees with OPC's position that the Company should recover no

part of the earnings-based incentive compensation in increased base rates, we agree with OPC's position that the Company should recover the equivalent to 100% target of the individual performance incentives in its AIP. (OPC Brief, p. 52)

Staff's reversal of position in its brief to now offer nothing above base salary is disappointing, and another example of Staff's lack of neutrality. (Staff Brief, p. 95) In response, the Company refers the Commission to the position taken in the Company's initial brief, including all cites to the record.

In its final note on the subject, Staff states that it is not attempting to reduce the total compensation for LAC and MGE employees; it just wants shareholders to pay compensation costs that show no tangible benefit to customers. (Staff Brief, p. 97) The flaw in this position is that Staff will simply not admit the fact that Spire Missouri's balanced incentive program has brought significant benefits to Missouri customers. Nor will Staff admit that, since the Company cannot continue to absorb millions of dollars in fair market compensation, in essence Staff is attempting to reduce employee compensation. Staff feels "sound public policy" would have the Commission disallow earnings based metrics on the belief that they align the employee with the shareholder and negatively impact customers. (Staff Brief p. 90) The Company challenges this belief and feels sound public policy would encourage the Company to further align the interests of the employee, shareholder and customer, rather than driving a wedge between them by pitting one against the other in a zero-sum game. Encouraging win-win situations generates a sustainable business model that benefits all stakeholders, and is sound public policy.

In the end, incentive compensation is simply part of a nearly universal market compensation package that employees expect to see and that Companies use to motivate performance. (Ex. 48, p. 5) Spire Missouri's AIP has a balanced level of financial and service

performance metrics that have created significant value for customers. (Ex. 5, pp. 7-8) We ask that the Commission maintain the policy it clarified in the 2009 Ameren case and approve recovery for Spire's reasonable compensation costs, including the costs of its balanced incentive compensation plans that better align the interests of employees with the business and customers.

IX. Uncollectibles

a. What is the appropriate amount of bad debt to include in base rates?

Public Counsel proposed in its brief that "the Commission order no change to Laclede's test year Uncollectible Accounts of $6,257,451 and MGE's test year amount of $1,755,577 for a combined $8,013,028 bad debt expense level." (OPC Brief at 47). For the reasons stated herein, OPC's position should be rejected.

OPC's position produces even less bad debt expense than the position espoused by Staff which has already been addressed in the Company's initial brief. (Company Brief at 112-14). OPC's brief adds little to the record to explain why the Commission should adopt the test year levels of bad debt expense when there have been substantial changes to the Company's write-off policy for both LAC and MGE.

While Staff used a normalized level of uncollectible expense by using a higher level than proposed by OPC, Staff's proposed approach produces a level that is still too low since the twelve-month period proposed by Staff is not long enough to fairly represent bad debt write off trends and fairly project future expense. An average of over at least three-years normalizes unusual variances that can occur in a shorter period such as twelve-months. Given the timing of the significant change in uncollectible policy, the Company believed that a sensible and practical solution was to use the three-year average for the period immediately prior to the change, which amount came to $13 million.

As explained in the Company's initial brief, the Company originally elected to use

an approach that would be easily understood and did not require detailed and complex workpapers to reconcile and normalize the post-change data to be comparable to the historical policy. However, the Company also reviewed a three, four, and five-year average approach. The Company believes that either the three year or five year average would provide a reasonable level of uncollectible expense in rates. However, OPC's test year levels of bad debt expense or the Staff's proposed levels should be rejected.

XI. Performance Metrics

a. Should a proceeding be implemented to evaluate and potentially implement a performance metrics mechanism? If yes, how should this be designed?

Based on its review of the initial briefs, the Company could not identify any party, other than the Company, that addressed this issue. The Company accordingly has nothing to add on this matter in this Reply Brief.

XXI. Transition Costs

h. Should LAC's and MGE's cost of service be adjusted to reflect the recognition of merger synergies through the test year?

In their Initial Brief, OPC and Staff oppose the modest synergy sharing proposals that have been presented by the Company in connection with the $19 million worth of savings achieved for Missouri ratepayers in connection with Spire's acquisitions of Alagasco and EnergySouth in 2014 and 2016. Importantly, neither dispute the Company's analysis that showed savings to Missouri customers. These savings resulted from the spreading of fixed costs, once borne almost entirely by Missouri customers, and now spread across Spire's larger business footprint. These savings are already included in these rate cases, but both parties vehemently oppose any mutually beneficial policy or further sharing of a modest portion of the

short-lived benefits the Company received for making these Missouri customer benefits happen.

In fact, OPC goes so far as to say that it is "audacious" for the Company to even ask for a sharing of these savings given the Company's asserted failure to seek Commission approval for the acquisitions and the results of the now discredited Staff Investigation Report filed on September 1, 2016. (OPC Initial Brief, pp. 53-55).

What is truly audacious is OPC's attempt to have the Commission's reject the Company's proposal on such specious grounds. Notably, OPC does not dispute the Company's contention that real savings were achieved as a result of these acquisitions and that they are currently included in the proposed cost of service in these proceedings. Nor does OPC take issue with the specific approaches that the Company has offered to quantify its share of such savings. Instead, OPC relies almost entirely on a complete corruption of the historical record regarding how OPC, the Staff and the Commission viewed these transactions at the time they were being done and on a Staff Investigation Report that has been proven to be grossly flawed from the date it was issued. They argue there has been no cost/benefit analysis done, relying upon the faulty conclusions of the Staff Investigation that Spire inappropriately charged acquisition costs to Missouri customers (they did not, as shown on pages 9-11 of the Response, filed September 6, 2016 in GM-2016-0342). However, the analysis shown in Company witness Lobser's surrebuttal testimony, Schedule CEL-S2, is net of costs allocated back to Spire Missouri, and there were no costs allocated to Missouri from the transactions, as noted above.

Turning to the first issue, OPC claims that the Company's proposal should be rejected because the Company did not come to the Commission to obtain approval for the Alagasco and EnergySouth acquisitions pursuant to its 2001 Holding Company Agreement in Case No. GM-201-342. (OPC Initial Brief p. 54). These belated claims of surprise and shock over the fact that Spire did not seek Commission approval for these transactions are growing old. As

explained in Exhibit 61, the language of the 2001 Holding Company Agreement is different from the language of the Great Plains Energy/KCPL Holding Company Agreement in a number of critical respects. (*Id*. at pp. 15-16).[4] Because of these differences, it did not, in the Company's view, require its parent, Spire to obtain Commission approval for the transactions involving acquisitions of utilities outside Missouri, unless such acquisitions would trigger certain jurisdictional events (which neither the Alagasco or EnergySouth acquisition did).

This was not just the Company's interpretation of the Holding Company Agreement but apparently it was also OPC's and Staff's interpretation of the Agreement prior to 2016. For example, at the very same time that the Company was seeking Commission approval to acquire MGE, its holding company was also seeking to acquire New England Gas. That intended acquisition of New England Gas was noted prominently in the application for approval of the MGE acquisition. Yet at no time during the multi-month approval process for the MGE acquisition did OPC or Staff ever mention a word about the Company or its parent needing Commission approval for the New England Gas acquisition. Silence reigned again in May 2014, when Spire's President and CEO, Suzanne Sitherwood discussed the intended acquisition of Alagasco in some detail during a formal, follow-up presentation to the Commission in Case No. GM-2013-0254. Again legal and technical representatives of both OPC and Staff were in attendance and none raised their hands or otherwise expressed the opinion that Commission approval for the acquisition was required. Nor did they do so for another year and a half until GPE was seeking approval of its acquisition of Westar. Only then did Staff and OPC begin to raise the Holding Company issue, since GPE had one as well, and start question for the first time whether the Company's Holding Company also required Commission approval for such

[4] Notably, the 41 words that make Section 5 of the Company's Holding Agreement different from KCPL's was omitted from the language cited by OPC in its Initial Brief.

transactions, notwithstanding its different language.

Given this historical record, the claims of outrage being expressed by OPC are misplaced and inappropriate and certainly do not constitute a basis for rejecting the Company's synergy sharing proposals. Nor do OPC's references to the 2016 Staff Investigation Report provide a reasonable basis for rejecting such proposals. As previously noted, the September 1, 2016 Staff Investigation Report regarding the effects of Spire's acquisition of Alagasco and EnergySouth in 2014 and 2016 and the news articles the OPC cites in its Brief and testimony gave the wholly incorrect impression that these acquisitions had "increased rates" and "decreased service" for the Company's Missouri customers.

As discussed in the Company's response to the Staff's Investigation Report, which is contained in Exhibit 61, these incorrect assertions were based on a summary in the Report that was fundamentally inconsistent with what the Staff's subject matter experts actually said in the Report. As the Response explained:

> The Staff's Report unfortunately contains an incorrect summary of its own experts' conclusions that falsely suggests that the Alagasco acquisition has had resulted in higher rates currently being charged and lower quality services currently being provided by Laclede Gas Company. This incorrect summary has, in turn, been relied upon by the media to misinform the customers of Laclede Gas and MGE into believing something that is simply not true - a result that unfairly tarnishes the reputation of Spire and Laclede Gas and does a real disservice to customers, employees and shareholders. What the Staff Report actually indicates is that:
>
> - The Staff has not identified any detrimental impacts on the quality of customer service being provided by Laclede Gasand MGE as a result of either the Alagasco or EnergySouth acquisitions.
>
> - The Staff has not identified any change in the rates currently being charged by Laclede or MGE as a result of either the Alagasco or EnergySouth acquisitions - a result that simply recognizes the fact that neither Laclede nor MGE have had a change in their base rates since these acquisitions occurred.
>
> - The Staff has identified a significant reduction in the level of

> administrative services being borne by Laclede Gas due to its ability to spread those costs over additional utilities -a benefit that will be shared with customers in an appropriate manner when rates are changed.
>
> In short, the information and conclusions provided by Staff's technical experts in the Report are in direct conflict with how those conclusions have been mischaracterized in the Report's Summary. Spire's efforts to grow a Missouri company are not only a refreshing departure from the serial takeover of companies that used to be headquartered in this state, but they are also actions that have and will continue to benefit the utility customers of its operating units through improved service and rates that are lower than they otherwise would have been. Staff's Report should not be allowed to suggest otherwise though an erroneous summary of its own findings. (Ex. 61, pp. 1-2).

The Company's characterization of the Staff's Report has been completely vindicated by the evidence presented in this proceeding. As the witness for the Staff acknowledged during the evidentiary hearing, however, there could have been no increase in rates relating to these acquisitions in 2016 because these are the first rate cases filed by the Company since those acquisitions took place. (Tr. 544, lines 16-23). Moreover, as the actual, undisputed evidence presented in these cases makes abundantly clear, rates will, in fact, be substantially lower, not higher, than would have otherwise been the case because of these acquisitions. And in contrast to what was said in 2016, not a single witness has been put forward in these cases to dispute or even question the Company's assertion that service has actually improved across a broad spectrum of service areas since those acquisitions occurred.

OPC should not be allowed to perpetuate these myths and clearly should not be allowed to rely on them to reject synergy sharing proposals that are based on the actual truth of what happened as demonstrated by the undisputed evidence presented in this proceeding. Instead, the Commission should approve whichever synergy sharing proposals made by the Company it believes is most appropriate, as one way of encouraging such mutually beneficial activities, especially with known and measurable customer benefits. Such action would also help to

correct, in a meaningful way, the historical record, which was so badly and unfairly distorted by Staff and now by OPC, of what was actually achieved by the Company in connection with these acquisitions.

For its part, the Staff opposes each of the Company's synergy sharing proposals for a variety of reasons, some valid, some not. First, the Staff opposes the alternative that was initially suggested by the Company to recover a portion of the transaction costs incurred to complete these acquisitions. The Staff argues that such transaction costs were incurred prior to the test year in this case and that recognizing them in the cost of service would constitute impermissible retroactive ratemaking. (Staff Initial Brief, pp. 103-104). Relying heavily on Staff witness Oligschlaeger, the Staff also asserts that the Commission has traditionally found that transaction costs (such as legal, investment banking, and similar fees) incurred to complete an acquisition should not be included in utility cost of service. (Staff Initial Brief, pp. 104-105).

The Company believes that the Staff makes a valid point regarding this alternative proposal and agrees that it should not be considered by the Commission as a way to permit the Company to retain a modest share of the synergies created as a result of the Alagasco and EnergySouth acquisitions. At the same time, however, the Staff has not offered any substantive reasons why the other alternatives proposed by the Company should not be approved by the Commission.

In fact, as discussed in the Company's initial brief (*see* pages 118-121), the synergy sharing alternative presented by Company witness Lobser in his surrebuttal testimony was based on Mr. Oligschlaeger's description of the framework that the Commission has used in the past to allocate the synergies and other savings achieved by utilities as a result of mergers or acquisitions. (Ex. 224, p. 16, lines 1-6; Ex. 8, pp. 13-15). The only adjustments that the Company has made to the framework described by Mr. Oligschlaeger is to: (a) forego recovery

of any transition costs (some or all of which a utility would typically be permitted to retain) and (b) to recognize half (rather than all) of the synergies that Company would have typically been permitted to retain through regulatory lag if these acquisitions had been completed at the beginning of the normal four-year cycle between rate cases. (Ex. 8, pp. 13-15).

While Staff quotes the very same testimony from Mr. Oligschlaeger in its entirety at page 105 of its Initial Brief, it offers no explanation of why this modest alternative for sharing the significant savings achieved in connection with these acquisitions is not fully in keeping with the Commission's long-standing practices in this area. The Company would submit that it is consistent with those practices and it, or one of the alternatives proposed by the Company that the Staff has not critiqued, should be approved. This would create mutually beneficial outcomes and support the further alignment of the business, employees and customers, creating more sustainable benefits for all stakeholders.

XIV. Customer Programs

The Parties have reached an agreement on all issues relating to its various customer programs, other than the amount of funding that should be authorized for its low-income affordability program (Issue XIV b. iv) and whether a certain amount of funding should be set aside for a pilot program aimed at installing combined heating and power projects in Missouri. (Issue XIV d.) Each will be addressed in turn.

b. Low Income Energy Assistance Program

iv. What is the appropriate funding level for each division?

The Company has proposed a funding level of $600,000 for LAC and $500,000 for MGE, but is open to a moderately higher level of funding should the Commission deem that to be appropriate.

TRUE-UP ISSUES

I. AMR Meters – LAC Only

a. What is the appropriate amount to include in rates to account for expenses related to LAC's purchase of automated meter reading ("AMR") devices?

b. What is the appropriate amount to include in the cost of service to account for property taxes related to the AMR meters?

Executive Summary: The Commission should include $1.1 million in rates to cover expenses related to LAC's purchase of AMR devices. This amount consists of $400,000 in property taxes and $700,000 in costs to maintain the system. In addition, the Commission should establish a new account for LAC's devices, being 391.2, and apply a 7.5-year remaining life amortization schedule reflecting an amortization rate of 13.3%.

Argument:

In this argument, Spire will address (i) the costs associated with the AMR purchase that should be allowed in rates; and (ii) the time period over which the AMRs should be amortized and the date by which LAC plans to replace the current AMR system.

This issue involves a transaction Spire Missouri voluntarily undertook during the true-up period so our customers could benefit from decreased costs, and so that the Company could be better positioned to negotiate a new agreement when the current agreement expires in 2020. (Tr. 2606, 2615, l. 3-22) In total the Company estimates the net benefit of this transaction to be about $1 million per year. Spire Missouri seeks an outcome under which the customers will reap the full $1 million per year, and the Company will net zero. In effect, the Company is asking for nothing on this issue. (Ex. 65, p. 2, l. 10-20)

Staff opposes the Company's position. Staff argues for a position in which customers will reap $2.1 million in annual savings and the Company will lose $1.1 million. If Staff's position is approved, the Company's good deed will not go unpunished. (Ex. 292, pp. 3-5)

The purchase of the AMR devices occurred on July 1, 2017, which is within the true-up period. The Company incurred costs during the true-up period and will continue to incur costs to maintain the system by replacing devices, and will also incur property taxes on devices valued at $16.6 million in July. The ongoing maintenance costs total about $0.7 million per year, and the annual property taxes will be about $0.4 million. (Ex. 65, pp. 1-2)

The standard for including costs in the true-up period is that they be known and measurable. The use of a true-up audit and hearing in ratemaking is a compromise between the use of a historical test year and the use of a projected or future test year. It involves adjustment of the historical test year figures for known and measurable subsequent or future changes. (*State ex rel. Mo. Pub. Serv. Co. v. Fraas,* 627 S.W.2d 882, 888 (Mo.App.W.D.1981)) The PSC has historically utilized the test year and true-up procedure to determine appropriate future rates because the historical test year's expenses can be used to determine reasonable future rates. *See e.g., State ex rel. Noranda Aluminum, Inc.,* 356 S.W.3d at 318 ("Past expenses are used as a basis for determining what rate is reasonable to be charged in the future in order to avoid further excess profits or future losses [....]"). (*Re: Kansas City Power & Light Company,* 509 S.W.3d 757 (W.D. Mo. 2016)

Including these costs in rates is also supported by the procedural order in this case, which identifies true-up items to include property taxes, capital costs, and other significant items to maintain a proper relationship of revenues, expenses and rate base. (Order Adopting Procedural schedule and Delegating Authority, May 24, 2017, p. 9)

These maintenance costs and property taxes are known and measurable. Regarding maintenance costs, Spire Missouri is well aware of the failure rate of the AMR units having worked with them since 2005. (Tr. 2616) Regarding property taxes, Spire Missouri can easily caluculate property taxes based on the value of the AMR device system and tax rates. (Ex. 65,

p. 3) The matching principle also supports inclusion. Customers were paying for these costs in rates via the $.98 per meter read charge. Customers have now received a huge discount, reducing the rate to $.24 per meter read, a cost that does not include system maintenance or property tax. It is appropriate to match these costs with the associated cost savings. After doing so, the customer retains reduced revenue requirement of $1 million. (Id., p. 2, l. 2-13)

Staff's rejection of property tax expense is particularly perplexing. It is a tax expense that is certain to occur, and at a very consistent rate. The property was purchased within the true-up period in 2017, and will be taxed based on a January 1, 2018 valuation. The only reason given by Staff not to approve such an expense is that it did not accrue until January 1, 2018, which is outside of the test year. (Ex. 292, p. 5, l. 9-17)

It was noted at the hearing that Spire Missouri's AMR purchase has increased its rate base which will increase its return. This is certainly true. Spire Missouri is also keeping eight months of cost savings wherein customers are paying about $.98 per meter read while Spire Missouri has paid only $.24 per read beginning on July 1. Eight months of these savings totals about four million dollars. (Tr. 2591-93) Of course during those same eight months, Spire Missouri is collecting nothing from, or on, its $16.6 million rate base investment while the asset amortizes on a 7.5-year schedule. (Tr. 2614, l. 11-16)

Had Spire Missouri waited until January 1 to make the deal instead of July 1, it would net the $1 million per year instead of the customer. (Tr. 2617) Spire Missouri is trying not to be that kind of utility. This issue boils down to what kind of regulatory environment we want to have in Missouri. The utility controls the timing of actions to a great extent (although not the filing of this rate case). The Company believes that encouraging utilities to take actions at a time that saves customers $1 million per year is good regulatory policy.

All of the parties involved in this issue agree that the Commission should authorize the

Company to place the AMRs into a new account, Account No. 391.2. The Company and Staff agree to an amortization period of 7.5 years for this account. This period reflects the fact that many of the AMR devices, which have a battery life of 15 years, have already been in service for 12 years. It also reflects the fact that Spire Missouri plans to move from an AMR system to an AMI smart meter network, sometime in the 2020-2024 time frame. OPC is again the outlier, seeking a depreciation rate of 5%, which reflects a 20-year life. (Ex. 65, pp. 5-6) There is absolutely no reason to assume a 20-year life for a network of AMR devices with a remaining life of about three years on average, on a system the Company intends to replace within six years.

CONCLUSION

For all of the reasons set forth above and in Spire Missouri's Initial Brief, the Company respectfully requests that the Commission resolve the remaining issues in these cases in a manner consistent with the Company's recommendations.

Respectfully submitted,

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ATTORNEYS FOR SPIRE MISSOURI INC.

CERTIFICATE OF SERVICE

I certify that a true and correct copy of the foregoing was served electronically, or hand-delivered, or via First Class United States Mail, postage prepaid, on all parties of record herein on this 17th day of January, 2018.

/s/ Marcia Spangler