

**BEFORE THE PUBLIC SERVICE COMMISSION
OF THE STATE OF MISSOURI**

In the Matter of the Verified Application and)	
Petition of Liberty Energy (Midstates) Corp.)	<u>Case No. GO-2014-0006</u>
d/b/a Liberty Utilities to Change its Infrastructure)	Tracking No. YG-2014-0004
System Replacement Surcharge.)	

STAFF BRIEF

COMES NOW the Staff (“Staff”) of the Missouri Public Service Commission (“Commission”), by and through counsel, and for its brief in this matter hereby states:

INTRODUCTION

In this case Staff investigated the *Verified Application and Petition* (“petition”) of Liberty Energy (Midstates) Corp. d/b/a Liberty Utilities (“Liberty” or “Company”) to change its infrastructure system replacement surcharge (ISRS), and ultimately recommended that the Commission approve Liberty’s petition to change its ISRS in accordance with the amounts shown in Staff’s hearing Exhibits 2 and 3. The Office of the Public Counsel (“Public Counsel”) opposed the ISRS petition and asked the Commission to reject it.

The evidence shows that Staff’s investigation was thorough. Staff conducted its investigation according to the legislature’s directions to the Staff in Section 393.1015.2 of the ISRS statute, and that investigation is the basis of Staff’s recommendation to the Commission, which is fully described in Staff’s *Updated Report*.¹ Because Public Counsel offers no specific monetary adjustments in the case, the Commission must decide whether to grant the petition in the amounts recommended by Staff, or deny the petition in its entirety.

As explained in this brief, the ISRS statute provides guidance to both Staff and the Commission about the scope of review in an ISRS case, and the statute also specifically provides

¹ Staff’s Exhibit 1. Staff’s Exhibits 2 and 3 supplement the *Updated Report* with Staff’s final recommended revenue requirement (Ex. 2) and rate design (Ex. 3).

that broad questions about the reasonableness and prudence of the infrastructure replacements—the very sorts of concerns presented here by Public Counsel—are to be addressed in the utility company’s next general proceeding.

PROCEDURAL HISTORY

Liberty filed its petition and tariff sheet on July 2, 2013, requesting an incremental ISRS revenue requirement increase of \$650,670.² On July 8, the Commission issued notice of the case, set an intervention date, and suspended Liberty’s tariff sheet (YG-2014-0004) until October 30,³ pursuant to the 120-day deadline in Section 393.1015.2(3). No party sought intervention.

On September 3, Staff filed its *Recommendation* pursuant to the statute’s 60-day deadline. The Office of the Public Counsel (“Public Counsel”) filed its *Motion for Order Rejecting or Denying Petition, or Order Setting an Evidentiary Hearing* on September 9. Prior to the hearing, the parties filed direct testimony on September 20, all of which was received into the record.⁴ Staff filed direct testimony in the form of its *Updated Report* on September 20.

The Commission conducted a hearing on September 26. At the hearing, Staff presented the final updates to its recommended revenue requirement and rate design in this case as Staff Exhibits 2 and 3. Those exhibits were received into the record.⁵

² Staff Exhibit 1, *Staff Updated Report on Infrastructure System Replacement Surcharge for Liberty Utilities* filed Sept. 20, 2013.

³ All dates 2013, unless otherwise noted.

⁴ Transcript, p. 36, ln 6; p. 52, lns 14-15; p. 73, lns 5-6; p. 91, lns 7-9.

⁵ *Id.*

ISSUES

The parties presented the following issues in this case:

1. Should the Commission approve an incremental ISRS (infrastructure system replacement surcharge) revenue requirement increase for Liberty Utilities in this case?
2. (i) What amount of incremental ISRS revenue requirement increase should the Commission approve for Liberty Utilities in this case (total and by district), and (ii) what composite/cumulative ISRS rate should Liberty Utilities be authorized to file for each customer class by district based on such increase?

The Commission should approve an incremental ISRS revenue requirement increase in the amount of annual pre-tax revenues of \$579,662 for Liberty in this case (consisting of \$30,432 for the WEMO District; \$178,799 for the SEMO District; and \$370,430 for the NEMO District), for a cumulative ISRS revenue requirement of \$1,332,023, as shown in Staff Exhibit 2. Staff Exhibit 3 shows Staff's calculation of the composite/cumulative ISRS rate that Liberty Utilities should be authorized to file for each customer class, by district. Liberty Utilities agreed to Staff's recommendation on these issues.⁶

These updated composite ISRS rates by district (on Staff Exhibit No. 3) are as follows:

<u>Northeast District</u>	<u>ISRS Charge</u>
Firm residential	\$3.16
Small Firm GS	\$3.16
Medium Firm GS	\$13.94
Large Firm GS	\$69.71
Interruptible Large Volume	\$69.71
<u>Southeast District</u>	
Firm Residential	\$1.04
Small Firm GS	\$1.04
Medium Firm GS	\$7.56
Large Firm GS	\$37.82
Interruptible Large Volume	\$37.82

⁶ Transcript p. 37 ln. 3.

West District

Firm Residential	\$1.97
Small Firm GS	\$1.97
Medium Firm GS	\$9.78
Large Firm GS	\$48.92

FACTS

Staff based the above recommendation on the following facts:

Rates ordered in Liberty’s most recent general rate proceeding, Case No. GR-2010-0192 took effect August 27, 2010. Rates related to Liberty’s previous ISRS case took effect November 2, 2012; in GM-2012-0037, Liberty adopted the then-effective ISRS authorized for Atmos Energy, which took effect February 14, 2011.⁷

In this case, Liberty initially filed a tariff sheet that would generate a total annual revenue requirement of \$650,670.⁸ The petition qualifies as a valid filing because the request exceeds “one-half of one percent (1/2%) of the natural gas utility’s base revenue level approved by the commission in the natural gas utility’s most recent general rate case proceeding.”⁹

Staff from the Auditing and Energy Units participated in the investigation of Liberty’s petition. The investigation included a review of the petition, all supporting documentation, Missouri statutory sections 393.1009, 393.1012 and 393.1015 RSMo. and all additional data provided by Liberty.¹⁰

Of the 275 distinct projects, Staff reviewed 36 work orders, covering a dollar amount of approximately \$2.2 million, which is about 58 percent of the amount requested by the company

⁷ *Id.* p. 3, ln 20 – p. 4, ln 2.

⁸ Staff Ex. 1, *Staff Updated Report*, p. 2, ln 17.

⁹ *Id.* p. 3, lns 12-16. This meets the requirements of Section 393.1012.1.

¹⁰ *Id.* p. 3, lns 8-11.

in its petition.¹¹ Staff's review included sufficient detail to show that the projects included replacement of either steel pipe or polyethylene pipe, and included some installation of either gas safety valves or excess flow valves.¹² Staff noted additional information concerning the age of the pipe being replaced and any corrosion or other defects.¹³ Staff reviewed the items to determine whether they led to an improvement in the integrity and safety of the system.¹⁴

Staff reviewed Liberty's project sub-ledger, which designated whether a project included material, supplies, overhead or labor, as well as whether the project was done for the integrity of the system, or for growth.¹⁵ Staff removed growth items.¹⁶ Staff testified that the costs included in the project number sub-ledger are detailed enough to understand the activities and costs incurred for each job.¹⁷

During its review, Staff identified several errors and omissions in the data provided by Liberty.¹⁸ Staff worked with Liberty and made adjustments to Liberty's application to address all the items Staff identified in its investigation.¹⁹

RESPONSE TO PUBLIC COUNSEL

Because Public Counsel has not proposed any specific adjustments to Staff's revenue requirement in this case, Public Counsel's argument presents the Commission with a stark choice: Approve the ISRS change in the amount recommended by Staff and agreed to by Liberty, or deny the petition. While Staff agrees with some of Public Counsel's concerns, they

¹¹ Transcript, p. 74, ln 22 – p. 75, ln 4.

¹² *Id.* p. 74, ln.22 – p. 75, ln 4.

¹³ *Id.* p. 79, lns 3-14.

¹⁴ *Id.* lns 19-23.

¹⁵ *Id.* p. 81 ln 25-p. 82 ln 8.

¹⁶ *Id.*

¹⁷ *Id.*

¹⁸ Staff Ex. 1, *Staff Updated Report*, p. 4 ln 11 – p. 11 ln 17.

¹⁹ *Id.* p. 4 lns 14-17.

do not justify a total rejection of a petition that Staff has found to comply with the ISRS statute. To do so would contradict the express language of the statute, and defeat its purpose.

A. State law provides direction on Staff’s review and the Commission’s approval of ISRS petitions.

Liberty bears the burden of proof on the issues in this case, because Liberty filed its petition requesting the Commission approve a change in its ISRS, and the burden of proof properly rests on the party asserting the affirmative of an issue.²⁰

Staff’s review is guided by the ISRS statute. Section 393.1015.2(2):

“The staff of the commission *may* examine information of the gas corporation to confirm that the underlying costs are in accordance with the provisions of sections 393.1009 to 393.1015, and to confirm proper calculation of the proposed charge, and *may* submit a report regarding its examination to the commission not later than sixty days after the petition is filed. **No other revenue requirement or ratemaking issues may be examined in consideration of the petition or associated proposed rate schedules filed pursuant to the provisions of sections 393.1009 to 393.1015.”²¹**

The Commission’s role is set forth in 393.1015.2(3) and (4):

“(3) The commission may hold a hearing on the petition and any associated rate schedules and shall issue an order to become effective not later than one hundred twenty days after the petition is filed.

(4) If the commission finds that a petition complies with the requirements of sections 393.1009 to 393.1015, the commission shall enter an order authorizing the corporation to impose an ISRS that is sufficient to recover appropriate pretax revenue, as determined by the commission pursuant to the provisions of sections 393.1009 to 393.1015.”

Section 393.1009(3) defines “eligible infrastructure system replacements” as “gas utility projects that: (a) Do not increase revenues by directly connecting the infrastructure replacement to new customers; (b) Are in service and used and useful; (c) Were not included in the gas

²⁰ *AG Processing, Inc. v. KCP & L Greater Missouri Operations Co.*, 385 S.W.3d 511, 514 (Mo. Ct. App. 2012), reh'g denied (Nov. 20, 2012).

²¹ Emphasis added.

corporation's rate base in its most recent general rate case; and (d) Replace or extend the useful life of an existing infrastructure."

Section 393.1009(5) states "gas utility projects" eligible for ISRS recovery may only consist of the following:

- (a) Mains, valves, service lines, regulator stations, vaults, and other pipeline system components installed to comply with state or federal safety requirements as replacements for existing facilities that have worn out or are in deteriorated condition;
- (b) Main relining projects, service line insertion projects, joint encapsulation projects, and other similar projects extending the useful life or enhancing the integrity of pipeline system components undertaken to comply with state or federal safety requirements; and
- (c) Facilities relocations required due to construction or improvement of a highway, road, street, public way, or other public work by or on behalf of the United States, this state, a political subdivision of this state, or another entity having the power of eminent domain provided that the costs related to such projects have not been reimbursed to the gas corporation;

When interpreting statutes, "the rules of statutory interpretation are not intended to be applied haphazardly or indiscriminately to achieve a desired result."²² Instead, "the canons of statutory interpretation are considerations made in a genuine effort to determine what the legislature intended."²³ The primary rule "is to give effect to legislative intent as reflected in the plain language of the statute at issue."²⁴ Statutory construction "should avoid unreasonable or absurd results."²⁵

²² *State ex rel. Union Elec. Co. v. Pub. Serv. Comm'n of Missouri*, 399 S.W.3d 467, 480 (Mo. Ct. App. W.D. 2013), quoting *Parktown Imports, Inc. v. Audi of Am., Inc.*, 278 S.W.3d 670, 672 (Mo. banc 2009).

²³ *Id.*

²⁴ *Id.*

²⁵ *State ex rel. Office of Pub. Counsel & Missouri Indus. Energy Consumers v. Missouri Pub. Serv. Comm'n*, 331 S.W.3d 677, 687 (Mo. Ct. App. 2011).

B. Noncompliance with a minimum filing requirement is not a sufficient basis under the statute to reject the petition.

Public Counsel argues that the Commission should reject Liberty’s petition because the initial filing did not contain citations to state or federal safety requirements. The issue of exactly what information gas companies must file pursuant to 4 CSR 240-3.265(20)(K) has never been litigated—similar ISRS petitions have not been challenged on these grounds.²⁶

If the Commission agrees with Public Counsel that Liberty’s initial filing did not comply with the rule, this should be considered a harmless error because Liberty subsequently provided citations in this case, as noted by Public Counsel in its *Motion*. Moreover, denial on these grounds may raise questions of lawfulness, because, as explained above, the statute states that the Commission “shall” grant the petition when it makes certain findings.

More broadly, the statute does not seem to support Public Counsel’s restrictive interpretation, which could undermine the purpose of the statute.

In defining “gas utility plant projects” eligible for ISRS recovery, Section 393.1009(5)(a) refers to certain pipeline system components that are “installed to comply with state or federal safety requirements,” and subsection (b) refers to certain projects that are “undertaken to comply with state or federal safety requirements.”

However, the statute does not define “state or federal safety requirements,” nor does the statute require that the petition include any citations to such requirements.

Commission Rule 4 CSR 240-3.265(20)(K) requires gas companies to file certain information along with petitions to establish, change or reconcile an ISRS, including “the specific requirements being satisfied by the infrastructure replacements” for each:

²⁶ *Direct Testimony of Mark D. Caudill*, p. 8, lns 17-18.

1. Mains, valves, service lines, regulator stations, vaults, and other pipeline system components installed to comply with state safety requirements;
2. Mains, valves, service lines, regulator stations, vaults, and other pipeline system components installed to comply with federal safety requirements;
3. Main relining projects, service line insertion projects, joint encapsulation projects, and other similar projects undertaken to comply with state safety requirements;
4. Main relining projects, service line insertion projects, joint encapsulation projects, and other similar projects undertaken to comply with federal safety requirements.

As explained above, Staff's analysis and adjustments confirmed, as instructed by statute, that the underlying costs accord with the ISRS statute and that the charge is properly calculated. Staff recommends that the Commission accept the results of Staff's analysis and find that the petition complies with the statute. If the Commission so finds, the statute requires the Commission to approve the petition. If the Commission determines that Liberty omitted required information in its original filing, that does not change Staff's recommendation that Liberty's petition, with Staff's adjustments, complies with the statute.

Staff agrees with Public Counsel—and the Commission—that the minimum filing requirements outlined in the rule significantly simplify the discovery process for all parties and aid Staff and Public Counsel in their analysis of ISRS petitions.²⁷ Liberty supplemented its filing in this case, however, so the omission would amount to harmless error, and therefore Staff cannot recommend complete denial of the petition, which it found to meet the statutory requirements for approval.

Moreover, Staff does not agree with Public Counsel's response to the citations that Liberty provided. In its *Motion for Order Rejecting or Denying Petition*, Public Counsel argued that Liberty's citations to certain portions of the Commission's Chapter 40 gas safety rules are

²⁷ *Order of Rulemaking*, Missouri Register Vol. 29, No. 8 p. 665, April 15, 2004.

not valid, because Public Counsel argues that “[t]he rules regarding gas leaks and maintenance expense do not *mandate* the type of replacement programs that the rule was meant to address....”²⁸

In its *Motion*, Public Counsel seems to argue that the statutory phrase “... to comply with state or federal safety requirements” means “a law that compelled Liberty to incur the expenses.”²⁹ However, no court has endorsed such an interpretation, and there does not seem to be statutory authority to support Public Counsel’s restrictive reading of the statute.

For example, Section 393.130 requires that “[e]very gas corporation... shall furnish and provide such service instrumentalities and facilities as shall be safe and adequate and in all respects just and reasonable.” This is arguably a “state safety requirement,” even though it does not tell a company when it *must* replace a *specific* piece of infrastructure.

The fact that the statute does not define “state or federal safety requirements” means that the Commission should not impose an artificially restrictive definition that defeats the purpose of the statute, because the Commission should “give effect to legislative intent as reflected in the plain language of the statute at issue.”³⁰

Furthermore, Public Counsel’s line of argument would seem to invite counter-productive litigation. The statute does not seem to contemplate arguments before the Commission about whether a specific piece of infrastructure is sufficiently “worn out” or “deteriorated” so as to justify replacement under a particular state or federal safety requirement, nor has the

²⁸ *Motion for Order Rejecting or Order Denying Petition, or Order Setting an Evidentiary Hearing*, p. 6. Emphasis added.

²⁹ *Id.*

³⁰ *Id.*

Commission ever rejected an ISRS application by engaging in such an analysis. Statutory construction “should avoid unreasonable or absurd results.”³¹

Staff does not recommend the Commission embark on a radically new interpretation of the ISRS statute in the context of this case, without a careful exploration of the potential consequences of such an interpretation.

C. The Commission has the statutory authority to approve a change in Liberty’s ISRS, because Liberty’s ISRS was initially approved within three years since the company’s last rate case, as required by statute.

Section 393.1012.2 provides that “[t]he commission shall not approve an ISRS for any gas corporation that has not had a general rate proceeding decided or dismissed by issuance of a commission order within the past three years...”

In this case Public Counsel reiterates its argument from Case No. GO-2013-0391. In that case, the Commission rejected Public Counsel’s interpretation of the statute.³² Staff’s argument on this issue, which the Commission adopted in Case No. GO-2013-0391,³³ is also the same. It rests on the statutory distinction between “establishing” and “changing” an ISRS.

Liberty’s most recent rate case was filed by Atmos Energy, Case No. GR-2010-0192, which was decided when the Commission’s *Order Approving Stipulation and Agreement* became effective August 27, 2010. The Commission established Liberty’s currently effective ISRS when it approved the application of Atmos Energy in Case No. GO-2011-0149, which became effective February 14, 2011.³⁴ Liberty adopted the currently effective ISRS authorized for

³¹ *State ex rel. Office of Pub. Counsel & Missouri Indus. Energy Consumers v. Missouri Pub. Serv. Comm’n*, 331 S.W.3d 677, 687 (Mo. Ct. App. 2011).

³² GO-2013-0391, *Order Approving Change in Infrastructure System Replacement Surcharge, Rejecting Tariff, and Approving New Tariff*, issued May 1, 2013, p. 5-6.

³³ *Id.*

³⁴ Staff Ex. 1, *Staff Updated Report* p. 4 lns 1-3.

Atmos Energy when Liberty acquired the assets previously owned by Atmos Energy in Case No. GM-2012-0037.³⁵

Therefore, the Commission *established* Atmos Energy's ISRS in February 2011, well within the three-year requirement of Section 393.1012.2. In this case, Liberty filed a petition to *change* its existing ISRS.³⁶ All arguments on this issue were fully developed in Case No. GO-2013-0391 and need not be repeated in complete detail here.

D. Liberty has met its burden of proving that the expenditures in its petition are lawfully eligible for inclusion in the ISRS.

Public Counsel's arguments on this point are not entirely clear. Public Counsel's *Motion for Order Rejecting or Denying Petition* argues that certain expenses are not eligible for inclusion because they cite to a safety statute which, in Public Counsel's view, does not "mandate" the expense. This argument was addressed above.

However, in Public Counsel's *Position Statement*, Public Counsel separates its arguments related to Liberty's compliance with the minimum filing requirements from its argument that Liberty has not met its burden of proof, stating only that "the evidence in this case will show that many of the expenses Liberty seeks to include in the ISRS are ineligible under Section 393.1009 RSMo." Yet, at this point, the evidence on which Public Counsel relies is not clear.

Public Counsel's witness Ted Robertson provided direct testimony which "attempted to verify the accuracy and reasonableness of the individual additions and retirement costs, and to 'highlight' several of the more obvious mistakes in the Company's calculation of the total ISRS

³⁵ *Id.*

³⁶ Section 393.1012 provides that "[i]n no event shall a gas corporation collect an ISRS for a period exceeding three years unless the gas corporation has filed for or is the subject of a new general rate proceeding. Section 393.1015.3 prohibits a gas corporation from changing its ISRS rate more than two times every twelve months. Liberty's compliance with those provisions of the statute is not at issue in this case.

revenue.”³⁷ The testimony asserts certain errors and omissions, then argues that “extrapolation of the possibility of similar errors... indicates that the ISRS revenues requested by Company are not an accurate representation of what should be authorized.”³⁸ However, instead of proposing a specific adjustment, Public Counsel apparently asserts that this “extrapolation” justifies complete denial of the petition.

Public Counsel’s testimony then identifies “other problems with Liberty’s processes” related to Liberty’s accounting, record-keeping and discovery. Again, Public Counsel does not propose any specific adjustments, but apparently asserts that these “concerns” should be grounds for complete denial of Liberty’s petition.

The statute does not support such a denial based on concerns and extrapolations. Quite the opposite—Public Counsel’s testimony seems to address exactly the kind of “ratemaking” issues the statute expressly reserves for Liberty’s next rate case.³⁹

Again, the ISRS statute confines Staff’s review to 1) confirmation that the underlying costs are in accordance with the provisions of the statute, and 2) confirmation of the proper calculation of the proposed charge. “No other revenue requirement or ratemaking issues may be examined in consideration of the petition or associated proposed rate schedules” filed pursuant to

³⁷ Transcript p. 4 lns 13-16.

³⁸ *Id.* p.9 lns 14-17, p. 10 lns 16-19.

³⁹ See Subsections 8 and 9 of Section 393.1015 RSMo, which state as follows:

8. Commission approval of a petition, and any associated rate schedules, to establish or change an ISRS pursuant to the provisions of sections 393.1009 to 393.1015 shall in no way be binding upon the commission in determining the ratemaking treatment to be applied to eligible infrastructure system replacements during a subsequent general rate proceeding when the commission may undertake to review the prudence of such costs. In the event the commission disallows, during a subsequent general rate proceeding, recovery of costs associated with eligible infrastructure system replacements previously included in an ISRS, the gas corporation shall offset its ISRS in the future as necessary to recognize and account for any such overcollections.

9. Nothing in this section shall be construed as limiting the authority of the commission to review and consider infrastructure system replacement costs along with other costs during any general rate proceeding of any gas corporation. (Emphasis added).

the ISRS statute. If the Commission finds that a petition complies with the statute, “the commission *shall* enter an order authorizing the corporation to impose an ISRS.”

Should the Commission deny Liberty’s petition on the grounds urged by Public Counsel, such denial could be unlawful. This is not to say that Public Counsel’s concerns are completely without merit—but the statute contemplates the Commission addressing those concerns in the rate case, during which all parties will have a full opportunity to investigate these concerns and propose resolution.

CONCLUSION

Both Staff’s investigation and Public Counsel’s investigation of Liberty’s petition raised concerns. Staff resolved its concerns by making specific adjustments to the petition, while Public Counsel states that its concerns remain unresolved and urges the Commission to reject the petition in its entirety. However, the Commission may not have statutory authority to deny the petition based on unresolved concerns. In fact, the statute contemplates that broad concerns over the Company’s accounting and record-keeping be addressed in the rate case. It would seem, in fact, that the process worked as intended in this case—Staff’s review satisfied the statutory instructions and opened a window into the Company’s operations that may inspire some further investigation in the Company’s next rate case, where the parties and the Commission may address all factors relevant to Liberty’s provision of utility service.

Should the Commission adopt Public Counsel’s arguments in this case, it would embark on a dramatic re-interpretation of the ISRS statute and diverge from the Commission’s treatment of ISRS cases for the past decade. Such a departure from past practice should be addressed in a workshop docket where all stakeholders may speak to ISRS issues, rather than in the context of a specific ISRS petition.

Therefore, Staff reiterates its recommendation that the Commission should issue an order in this case that:

1. Rejects the ISRS tariff sheet filed by Liberty on July 2, 2013;
2. Approves Staff's determination of the incremental ISRS surcharge revenues in the amount of annual pre-tax revenues of \$579,662, consisting of \$30,432 for the WEMO District, \$178,799 for the SEMO District, and \$370,430 for the NEMO District;
3. Authorizes Liberty to file an ISRS rate for each customer class by district as reflected in *Schedule JM-1 Updated* (Staff Exhibit No. 3, page 2 of 2); and
4. Approves Liberty's request for waiver of the 60-day notice requirement for contested cases.

Respectfully Submitted,

**STAFF OF THE MISSOURI
PUBLIC SERVICE COMMISSION**

/s/ John D. Borgmeyer

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CERTIFICATE OF SERVICE

I hereby certify that true and correct copies of the foregoing were served electronically to all counsel of record this 4th day of October, 2013.

/s/ John D. Borgmeyer