

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

In the matter of The Empire District)
Electric Company of Joplin, Missouri for)
Authority to File Tariffs Increasing Rates)
for Electric Service Provided to)
Customers in the Missouri Service Area of)
the Company.)

File No. ER-2012-0345

EMPIRE’S POST-HEARING REPLY BRIEF

COMES NOW The Empire District Electric Company (“Empire” or “Company”), by and through counsel, and for its Post-Hearing Reply Brief in further support of its request for rate relief and in response to the briefs filed herein on September 20, 2012, by the Midwest Energy Users’ Association (“MEUA”), the Staff of the Commission (“Staff”), the Office of the Public Counsel (“Public Counsel”), and the Midwest Energy Consumers Group (“MECG”), respectfully states as follows to the Missouri Public Service Commission (the “Commission”):

The issue before the Commission is whether or not Empire’s interim tariff, designed to generate approximately \$6.2 million on an annual basis, subject to refund, should be approved at this time. There appears to be no question regarding the Commission’s authority to grant interim rate relief. Instead, the fundamental dispute between the parties in this case involves the legal standard to be applied by the Commission in assessing Empire’s rate increase request.

At page five of its brief, MECG urges the Commission to “maintain its reliance upon the emergency standard in assessing the propriety of interim rates.” On page one of its brief, Public Counsel states that the “bottom line is that Empire is not facing an emergency or near emergency situation . . .” MEUA argues at the outset of its brief that “interim relief for a Missouri utility is appropriate when it is necessary to maintain the economic life of the utility so that it can continue to provide service to the public.” Staff argues at page five of its brief that the grant of

interim rate relief is discretionary, but that the Commission's discretion should only be exercised "where a showing has been made that the rate of return being earned is so unreasonably low that it establishes a deteriorating financial condition which would impair the utility's ability to render adequate service or to maintain its financial integrity."

It is the position of Empire, however, that the Commission must consider the Company's rate increase request, not under any so-called "emergency standards," but pursuant to RSMo. §393.150. Contrary to the claim of MECG at pages 14-20 of its brief, Empire is not urging the Commission to apply some sort of "extraordinary circumstances" test to the Company's request for rate relief. On the contrary, Empire seeks rate relief pursuant to §393.150.2. That statute simply provides that "(a)t any hearing involving a rate sought to be increased, the burden of proof to show that the increased rate or proposed increased rate is **just and reasonable** shall be upon the gas corporation, electrical corporation, water corporation or sewer corporation, and the commission shall give to the hearing and decision of such questions preference over all other questions pending before it and decide the same **as speedily as possible**." (emphasis added) This statutory language, which prescribes the standard to be applied in this case, is clear and unequivocal.

RSMo. §393.150 does not distinguish between "interim" or "permanent" rate increases. The statute does not qualify the granting of rate relief only in "emergency" circumstances. In establishing just and reasonable rates, the Commission "must stay within 'the ambit of [its] statutory authority.'" *State ex rel. Missouri Water Company v. PSC*, 308 S.W.2d 704, 718 (Mo. 1957).

The case of *State ex rel. Laclede Gas Co. v. Public Service Commission*, 535 S.W.2d 561 (Mo.App. 1976), is often pointed to as authority to apply an emergency standard when

considering “interim” rate relief requests. In that case, however, the Commission was concerned with an application and not a tariff filing subject to suspension. This distinction is critical. Section 393.150 clearly provides that any rate increase request, after suspension of the tariff, places upon the utility the burden of demonstrating that the proposed rate is just and reasonable. Furthermore, the Court’s reference to “discretion” in Laclede concerned the latitude the Commission has regarding whether or not to suspend a tariff or to allow the tariff to become effective by operation of law on a date sooner than that required for a full hearing. When a tariff is suspended and set for hearing, §393.150 controls and “discretion” with regard to possible suspension is no longer a question before the Commission.

It is also noteworthy that §393.150 allows for suspension of a tariff for up to 120 days, plus an additional six months, but the statute does not mandate or guaranty suspension for that length of time. As noted, to the contrary, §393.150.2 actually requires the Commission to decide the issue “as speedily as possible.”

Staff asserts that Empire is urging the Commission to apply this “just and reasonable” standard for rate relief without consideration of all relevant factors. (Staff Brief, p. 1) All relevant factors are taken into account, however, by Empire’s actual earned common equity return, which, in 2011 was 7.9% and as of June 30, 2012, was down a notch to 7.8 percent.¹ (Ex. 3, p. 7; Ex. 4, Sch. RWS-1 which compares Empire’s authorized return on equity vs. Empire’s actual return on equity for the period shown indicates that at the end of 2011 the Company’s actual ROE was 7.90%. Trans. Vol. 2, p. 113)² Moreover, which factors are “relevant” in a rate

¹ The common equity return should not be confused with an overall rate of return. (See Sager Direct, Ex. 4, p. 3 where Empire’s proposed weighted (overall) rate of return in this case is 8.32%)

² Revenue requirement is calculated by adding the company’s operating expenses, its depreciation on plant in rate base, taxes, and its rate of return multiplied by its rate base. The revenue requirement can be expressed as the following formula:

$$\text{Revenue Requirement} = E + D + T + R(V-AD+A)$$

case is a decision for the Commission. Pursuant to RSMo. §393.270.4, the Commission “may consider all facts which in its judgment have any bearing upon a proper determination of the question.” The Commission is not bound by a certain list of factors in assessing Empire’s rate relief request. “Each case must be determined upon its own facts and, oftentimes, varying factors that may be peculiarly relevant to a reasoned determination of the issue of ‘just and reasonable’ rates under conditions then existing.” *State ex rel. Missouri Water Company v. PSC*, 308 S.W.2d 704, 718 (Mo. 1957). The Commission, within the limits of its statutory authority, may “make such pragmatic adjustments in the rate making process as may be indicated by the particular circumstances in order to arrive at a just and reasonable rate.” *State ex rel. Valley Sewage Company v. PSC*, 515 S.W.2d 845, 850 (Mo.App. 1974).

At pages 12-13 of its brief, Staff asserts that Empire presented testimony dealing with only two issues: revenues experienced during the 2011-2012 winter months and capital invested and expenses incurred to restore service following the Joplin tornado. In reality, however, and as noted in Empire’s initial post-hearing brief, the following Empire testimony was admitted into evidence in this case for purposes of consideration of Empire’s interim rate increase request which testimony details evidence on a variety of matters in addition to those related to the tornado:

- Empire Ex. 1 - Direct Testimony of Brad P. Beecher;

Where: E = Operating expense requirement
D = Depreciation on plant in rate base
T = Taxes including income tax related to return
R = Return requirement
(V-AD+A) = Rate base

For the rate base calculation:

V = Gross Plant
AD = Accumulated depreciation
A = Other rate base items

(In the Matter of Missouri Gas Energy’s Tariffs to Implement a General Rate Increase for Natural Gas Service, Case No. GR-2004-0209, Report and Order issued September 21, 2004)

- Empire Ex. 2 - Direct Testimony of Kelly S. Walters;
- Empire Ex. 3 – Interim Surrebuttal Testimony of Kelly S. Walters;
- Empire Ex. 4 - Direct Testimony of Robert W. Sager;
- Empire Ex. 5 - Direct Testimony of Scott Keith; and
- Empire Ex. 6 - Direct Testimony of Joan E. Land (p. 1, lines 1-15; p. 9, line 15 – p. 10, line 10).

Of significance is the unchallenged testimony that Empire's rate of return was 7.8 percent as of June 30, 2012, and that this rate of return takes all elements of Empire's cost of service into account. (Trans. Vol. 2., p. 113, lines 18-25; Ex. 3, p. 7; see also Ex. 4, Sch. RWS-1 which indicates an actual earned return on common equity of 7.9% for 2011) The Commission has the authority and obligation to determine which portions of the evidence now in the record in this proceeding are relevant to Empire's rate increase request.

Empire's Electric Interim Rider INT, consisting of five tariff sheets, is designed to increase the Company's gross annual electric revenues by \$6.2 million subject to refund, a just and reasonable interim increase under the circumstances presented. The interim request represents approximately 21 percent of the Company's overall revenue increase request of \$30.7 million. (Ex. 2, Walters Direct: p. 6)

While the amount of Empire's interim rate request was calculated based upon the impacts of the Joplin tornado, the actual underlying basis for the calculation should not necessarily determine the outcome. Stated another way, the interim request should not be considered only in light of the May 2011 tornado. While Empire has shown through its evidence that it has expended over \$27.6 million as a result of the tornado, this expense is not the only factor that has led to Empire's low rate of return. Empire's evidence also demonstrates that it is currently experiencing a \$30.7 million revenue deficiency. (Ex. 1, p. 4; Ex. 2, p. 4) Possible offsetting items to the tornado-related costs in other components of Empire's revenue requirement

calculation are taken into account in Empire's 7.8% common equity return. The interim request, \$6.2 million, is only about 21% of the overall request. (Ex. 2, p. 6)

There is no evidence to suggest that a \$6.2 million revenue increase, whatever its basis, would increase Empire's actual earned return to a point that would be considered to be unreasonably high. Thus, any basis for the \$6.2 million level of rate increase would support Empire's request in this case. In this regard, Empire's "permanent" rate request in the amount of \$30.7 million is driven by the following key components:

Description	Revenue Requirement
Tornado	\$ 6.2
SPP Transmission Charges	4.3
Retirement Riverton 7 & 8	3.2
Systems Replacement (ERP)	3.2
Vegetation Management	4.2
Depreciation Expense	2.5
General and Administrative	4.7
Other	<u>2.4</u>
Total Base Rates	\$ 30.7

(Ex. 2, p. 4)

While the focus here has been on item 1, the tornado, with a \$6.2 million revenue requirement, the other items may be considered as well.

In any event, with regard to the tornado:

- Empire has invested over \$27.6 million to replace the electric infrastructure destroyed by the tornado, with estimated carrying costs of approximately \$4.5 million (Empire Ex. 2 – Walters Direct: p. 10);
- Empire's overall customer count in Missouri remains down by slightly over 1,400 customers (Empire Ex. 2 – Walters Direct: pp. 10-11);

- The interim rider is designed to recover the above two components of the revenue requirement associated with the May, 2011 tornado (Empire Ex. 2 – Walters Direct: p. 11);

In addition, the following facts are critical:

- Empire does not have an opportunity to earn its authorized return. In those cases over the last ten years where the Commission made findings concerning Empire's common equity rate of return ("ROE"), the Commission authorized ROEs for Empire of 11% in 2005, 10.9% in 2006, and 10.8% in 2009. However, Empire's highest earned common equity return over the last ten years was only 8.4% -- and that occurred in 2006. (Empire Ex. 4 – Sager Direct: Sch. RWS-1 which compares authorized ROE's vs. actual ROE's for the period shown).
- Empire's opportunity to earn a fair rate of return has been impaired since the tornado struck Joplin in May 2011. The continuing impacts of the tornado (lower customer levels and deferred tornado related costs) have yet to be reflected in Empire's rates and will continue to exist and grow, respectively, until they are reflected in rates. (Ex. 3, Walters Interim Surrebuttal Testimony, p. 7)
- It is undisputed that Empire lost several thousand customers as a result of the tornado. While the hotter than normal weather and influx of temporary rescue and assistance workers mitigated some of the impact in terms of the electric sales Empire lost due to the destruction of the Company's customer base in Joplin in the summer of 2011, there is no doubt that Empire's electric sales in Joplin were adversely impacted by the tornado. The loss of customers was in the thousands and had those customers been able to take electric service in the summer of 2011

and the winter of 2012, Empire's electric sales would have been significantly higher. (Ex. 3, Walters Interim Surrebuttal Testimony, p. 11)

- Empire's earned rate of return, which takes all elements of Empire's cost of service into account, was 7.9% in 2011 and 7.8 percent as of June 30, 2012 (Trans. Vol. 2., p. 113, lines 18-25; Ex. 4 Sager Direct, Sch. RWS-1; Ex. 3 – Walters Surrebuttal: p. 7); and
- The money collected under the interim tariff would be subject to ratepayer refund with interest pending the Commission's final determination in the "permanent" case (Empire Ex. 5 – Keith Direct: Sch. WSK-4).

The briefs filed by the other parties herein focus on the "emergency" standard and the application of the facts of this case to that standard. As this is not the legal standard to be applied in this case, Empire will not respond to many of the specific arguments set forth in those briefs. There is one glaring factual inaccuracy, however, that Empire believes warrants attention. At page 14 of its brief, MEUA incorrectly states that Empire witness Beecher testified that *he* received incentive compensation of \$250,000 following the Joplin tornado. In reality, however, Mr. Beecher testified that \$250,000 was paid in 2011 to the officer *group* – not to any individual officer, and that the payment was roughly half of the traditional amount. (Tr. Vol. 2, p. 92)

Empire would also like to address the arguments that have been made suggesting that the Company should not be awarded rate relief at this time because it is still able to provide safe and adequate service. First, this is not the standard for rate relief to be applied in accordance with §393.150. Second, the Missouri Court of Appeals has clearly stated that in setting new rates for a utility, the Commission need not wait for the utility to be on the brink of financial collapse.

We do not believe that the Commission was constrained to wait until Empire was on the brink of literal financial collapse before exercising its authority to ensure

the welfare of the public by protecting the viability of the utility. For example, the Commission found that "Empire's corporate credit rating by Standard and Poor's was downgraded, on May 16, 2006 from BBB to BBB-, the lowest investment grade rating" and that prior to February 13, 2006, Empire was on "a negative credit watch." We believe that this is just further evidence to support the above findings and conclusions.

Ultimately, because OPC concedes that the Commission has a duty to ensure the viability of public utilities to *protect the public*, we must reject its argument on appeal that raising rates is inherently contrary to the safety and welfare of the public.

State ex rel. Praxair, Inc. v. PSC, 328 S.W.3d 329, 345 (Mo.App. W.D. 2010). The same court also noted that the Commission is not bound to any set methodology in ensuring a just and reasonable return in setting rates, that the Commission has considerable discretion in rate setting due to the inherent complexities involved in the rate setting process, and that it is not the theory or methodology that is significant, but the impact of the rate order which counts. *Id.* at 339.

The Commission suspended Empire's proposed Rider INT, the parties agreed upon a procedural schedule, and an evidentiary hearing has been held before the Commission. The Commission must now issue its rate order ensuring just and reasonable rates for Empire and its electric customers in accordance with §393.150. Fortunately, Empire and its shareholders were able to make financial and other sacrifices to ensure that the Company's customers were able to continue to receive safe and reliable service following the tornado. Empire's rates, however, no longer can be considered to be just and reasonable. That is because the costs incurred in connection with the tornado, which are being deferred pursuant to an accounting authority order ("AAO") issued by the Commission in Case No. EU-2011-0387, and the losses in terms of customers served, were not, and have yet to be, reflected in Empire's ongoing cost of service and revenue requirement, and because Empire is not earning anywhere near its authorized common equity return or any reasonable return.

Lastly, Empire would like to respond to the argument that Empire is simply seeking a rate increase to increase the Company's profits. Public Counsel states at page three of its brief that "no Public Service Commission in Missouri's history has granted an interim increase simply to increase a utility's profits." Empire seeks a rate increase at this time because the Company has made expenditures as a result of the tornado that are not reflected in rates; is experiencing a decline in revenue due to the loss of customers; has a revenue deficiency as a result of other items; and does not have the opportunity to earn anywhere near its authorized return or what can reasonably be characterized as an appropriate return. The "interim" request is for a \$6.2 million portion of the "permanent" request of \$30.7 million. The revenues collected will be subject to refund, thereby protecting Empire's customers. Stopping the deferral authorized by the AAO now also means that fewer expenses will be deferred or added to capital, therefore reducing the asset base. A smaller asset base means less to earn on and, thus, lower associated rates for Empire's customers. All else being equal, granting the interim request will reduce the permanent revenue requirement associated with the deferral, thus lowering the overall cost to Empire's customers. These facts demonstrate that Empire's proposed rate is just and reasonable.

The Commission has a rate case before it. Empire's proposed Interim Rider INT meets the statutory "just and reasonable" standard and, in accordance with §393.150, should be approved by the Commission at this time.

WHEREFORE, Empire hereby submits the foregoing post-hearing brief in support of its request for rate relief in the amount of \$6.2 million, to be implemented through the proposed Rider INT, to remain in effect until the "permanent" rates to be authorized by the Commission in this case become effective, and to be subject to refund.

Respectfully submitted,

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ATTORNEYS FOR THE EMPIRE
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CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the above and foregoing document was sent via electronic mail on this 1st day of October, 2012, to all parties of record.

